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The Political Economy of Business Bailouts

Volume 2

ONTARIO ECONOMIC COUNCIL RESEARCH STUDIES

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This report, printed after the Ontario Economic Council disbanded in late 1985, reflects the views of the author and not necessarily those of the Council. The Council established policy questions to be investigated and commissioned research projects, but it did not influence the conclusions or recommendations of authors. The decision to sponsor publication of this study was based on its competence and relevance to public policy and was made with the advice of anonymous referees expert in the area.

Contents

Preface to case studies

The following fifteen case studies comprise fourteen studies of government attempts to assist particular firms in serious financial difficulties and one study of more significant bailouts handled programmatically under the federal Enterprise Development Program (EDP), administered by the former Department of Industry, Trade and Commerce (now the Department of Regional and Industrial Expansion). Data for the latter was kindly provided in nonidentifiable form by officials from the EDP. The remaining firm-specific studies (some of which are also reflected in the EDP data) were initially prepared from public sources, and drafts were then submitted to government and corporate officers involved in the cases. We have attempted to ensure that those case studies are accurate and current as of December 1984. Unfortunately, current government policy on case studies of government decision-making precluded personal interviews with government officials involved in the bailouts under study. This constraint substantially limited our ability to describe the decision-making process and to analyse the influences that shaped the outcomes. However, subject to this constraint, we gratefully acknowledge the co-operation and assistance of many government and corporate officials, especially officials in the Department of Industry, Trade and Commerce.

We also gratefully acknowledge the invaluable contributions of Ann Peel, Barbara Quinn, and Wendy Rotenberg in the research and writing of these case studies.

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Volume 2

1
Chrysler Canada Ltd.

INTRODUCTION

Chrysler Canada is a wholly owned subsidiary of Chrysler Corporation of Detroit, USA.[1] Decisions on most aspects of production, marketing, operations, and research and development are controlled in Detroit. In 1979 Chrysler Canada was Canada's eighth largest industrial company,[2] and one of the 'Big Four' of the auto industry, a category which includes Ford, General Motors, and the American Motor Company. Chrysler Canada has historically held third place in terms of market share, although it moved into second in September 1981.[3] Its market share of 17 per cent[4] in Canada is higher than that of Chrysler Corporation in the United States.[5]

In 1978 Chrysler Corporation faced its first revenue loss due mainly to high inventories and poor sales in the United States. In addition, the company blamed its increasingly apparent financial difficulties on US government energy regulations. It claimed that their equal application to all companies placed Chrysler at a competitive disadvantage with Ford and General Motors which were able to spread their fixed retooling costs over a larger market share. Even American Motors was not as hard hit because it had limited product lines and hence smaller retooling costs.

As indicated in Table 1 Chrysler's liquidity shows a steady deterioration; the current ratio fell from 1.56 in 1978 to 1.28 in 1981. Chrysler's coverage of interest and preferred dividends was also very poor during this period. Poor earnings and turnover contributed to a

TABLE 1
Financial Statistics, Chrysler Canada Ltd.

	1983	1982	1981	1980	1979	1978	1977
1. Current ratio	1.12	1.40	1.28	1.35	1.43	1.58	1.56
2. Quick ratio	.77	.91	.88	.84	.93	1.07	1.12
3. Z	3.04	(.01)	(.60)	(1.24)	(.69)	.23	1.65
4. EBIT/(interest and preferred dividend) .5	5.18	1.47	(.64)	(4.46)	(3.08)	(3.31)	3.04
5. EBIT/(average total assets)	.24	.07	(.03)	(.21)	(.06)	(.043)	.023
6. Net income/sales	.03	.01	(.02)	(.09)	(.03)	(.01)	.02
7. Sales/average total assets	5.21	5.08	3.53	2.74	3.09	3.49	2.22
8. (6)(7) = Dupont ROA	.14	.02	(.08)	(.25)	(.11)	(.04)	.04
9. Debt/(common and preferred)	3.29	14,920.72	6,076.85	19.25	.81	.13	.15

SOURCE: Calculated from data from the Financial Post Corporation Service, 30 October 1984 and Chrysler Canada Financial Statements.

negative return on investment from 1978 to 1981. Chrysler's leverage problems were intensified in 1981 and 1982 as losses continued to erode equity. Chrysler's Z score shows that the company was classified as bankrupt from 1977 to 1982.

Chrysler Canada financial statements reported in 1979 that the company was in violation of its debt covenants and hence technically in default. The debt exposure of the various Canadian banks as of 1981 in US dollars was: Bank of Montreal $67 million, Royal Bank $48 million, Canadian Imperial Bank of Commerce $41 million, Toronto Dominion $36 million, and the Bank of Nova Scotia $33 million.[6]

Chrysler Canada's difficulties were also reflected in employment statistics as shown in Table 2.[7] In 1977 Chrysler employed 16,000 workers in Ajax, Windsor, and Etobicoke. Approximately 12,000 were employed in Windsor where the majority of Chrysler's Canadian operations are located.[8] By 1981 Chrysler's total workforce had dropped to a low of 9,255, rising again to 11,300 by 1983. However, this decline must be viewed in the context of substantial declines that occurred throughout the auto industry, especially in Windsor.

TABLE 2
Chrysler employees in Canada, 1977-1983

1977	1978	1979	1980	1981	1982	1983	1984
16,000[a]	14,738[a]	12,727[b]	10,300[c]	9,255[d]	11,175[e]	11,300[f]	12,500[g]

SOURCES:
a *Financial Post* 31 January 1979.
b *Globe and Mail* 25 August 1979.
c *Globe and Mail* 25 March 1979.
d *Financial Post* 31 January 1981.
e *Toronto Star* 30 June 1982.
f *Globe and Mail* 27 April 1983. Figures provided by the Ontario Ministry of Labour as of 4 May 1983 indicated that the number of employees was 9,140 when one excludes those on temporary layoff. The number on temporary layoff in earlier years is not available for comparison purposes.
g Interview with Chrysler official, January 1984.

In May 1980 Chrysler (Canada) Ltd., became party to a loan-guarantee agreement with the federal government. Previous assistance to Chrysler had been in the form of local and provincial tax incentives for the location of new plants. Federal assistance was granted through the Industry and Labour Adjustment Program (ILAP) administered by the Department of Industry, Trade and Commerce. ILAP is designed to aid industrial sectors most affected by technical change and foreign competition, such as the automobile industry which was strongly affected by growth in Japanese imports. Ontario's aid was granted on an *ad hoc* basis in response to the employment crisis in Windsor. It appears that employment was the dominant concern of both governments. Given the depressed labour market in the auto industry around 1980, it was perceived that Chrysler's bankruptcy was likely to have a crippling effect on Windsor (an area represented by three Liberal cabinet ministers). General Motors and especially Ford were also experiencing dramatic sales and employment declines; the problems were not unique to Chrysler.

Chrysler has not drawn on the loan guarantee and has since restored a healthy level of profitability.

RAMIFICATIONS OF CHRYSLER'S DECLINE

Consequences to the community

Chrysler Canada's main operations are in Windsor, Ontario; however, there is also a trim plant in Ajax and an aluminum-casting plant in Etobicoke. Chrysler is Windsor's largest employer, having employed 7 per cent of the city's 150,000 member labour force in 1981.[9]

In 1977-8 Windsor experienced a boom in residential real-estate values, and the general economic climate was optimistic.[10] By 1979 housing prices were falling, as documented by Robert Richardson, general manager of the Windsor Chamber of Commerce. A house that was valued at $58,000 in 1978, had dropped to $55,000 by August 1979.[11] Retail sales of consumer goods continued to do well until late 1980 when the Supplementary Unemployment Benefits (SUB) fund ran out.[12] Unemployment levels reached 16.9 per cent in April 1983, having climbed from 12.3 per cent in 1980.[13] In June 1980 there were 21,228 registered unemployed with no realistic expectations of obtaining work.[14] In November 1979 the *Financial Post* quoted an internal report by the Ontario Ministry of the Treasury and Economics to the effect that a Chrysler bankruptcy would push unemployment in Windsor to 40 per cent with 15,000 direct and 30,000 indirect jobs lost.[15] Herb Gray forecast that 14,000 jobs would be lost in Windsor, Ajax, and Etobicoke and a further 16,000 jobs in 600 dealerships would be terminated if Chrysler failed.[16] In addition, Chrysler pays approximately $4 million per year in local taxes which amounts to 3 per cent of Windsor's annual tax receipts.[17]

The Mayor's Committee on Services for the Unemployed reported in 1980 that the demand for social services had risen 400 per cent since 1979.[18] Family stress, alcohol and drug dependence were the most common problems.

Banks and mortgage firms extended credit to individuals by temporarily waiving interest payments,[19] and banks made available 'equity loans'. Under this arrangement homeowners were permitted to use the equity in their homes as security for a loan to pay the mortgage interest. Measures such as these helped to contain the rate of default on consumer loans and charge accounts at 14 per cent, with the mortgage-default rate at a lower level. The Central Mortgage and Housing Corporation (CMHC), which holds 3,000 mortgages in Windsor, reported in 1980 that it had foreclosed on only five homes in recent years.[20] This was in part due

to the expense of foreclosure, involving legal fees, insurance costs, and the difficulty of resale in a depressed region. It also became apparent from press reports that measures such as those by the banks were carried out in the expectation of future prosperity. Although the layoff levels of the past few years were unprecedented, the community was accustomed to fluctuating production schedules and their effect on the economy.

Workers affected

Press and government sources do not focus on specific demographic data dealing with characteristics of the workforce. However, data provided by Chrysler Canada (Table 3) indicates some such characteristics. The majority of employees are married, male, hourly production workers and they are well paid relative to workers in other industries. Their average age is slightly under forty and their years of service are quite high (eleven to thirteen years) and rising, reflecting the effect of seniority on layoffs.

As of 1983, press reports indicate that employment at Chrysler includes 7,385 unionized hourly employees and 1,755 managerial.[21] Chrysler Canada's labour costs were on average approximately $7.00 per hour less than the Americans due to the exchange rate and lower costs for health benefits. Prior to the December 1982 collective agreement the average hourly wage was $9.00[22] which had risen to $10.79 over 1983.[23] Chrysler's unionized employees, which include a portion of salaried staff, belong to the United Auto Workers of America.

Under a program initiated in 1979 by Lloyd Axworthy, then federal Minister of Employment and Immigration, auto workers in Windsor were eligible for extended Unemployment Insurance benefits for up to fifty-two weeks. A Canada Works Program was established to provide the necessary ten-weeks employment for extension eligibility. However, maximum UIC benefits are $174.00 per week and Supplementary Unemployment Benefits (SUB), whose purpose is to restore workers to approximately 90 per cent of their wage level, were running out as early as July 1980.[24]

Human-interest articles in the press focused on the plight of desperate families placing their hopes for the future on a bailout.[25] Every month in 1980 approximately 200 workers were leaving Windsor for western Canadawith the majority returning due to the lack of demand for skilled labour.[26] Numbers of those leaving the workforce for retirement or re-

TABLE 3
Characteristics of Chrysler Canada's workforce 1979, 1980, 1983

	Dec. 1979	Dec. 1980	June 1983
Employment, hourly	9,685	7,604	9,418
Hourly skilled	941	667	787
Hourly production	8,744	6,937	8,631
Employment, salaried	2,289	1,850	1,996
General salary	841	653	726
Management	1,448	1,197	1,270
Total employment[a]	11,974	9,454	11,414
Proportion female			
Hourly	9.0	9.8	10.7
Salary	14.8	14.3	n/a
Average years service			
Hourly	11.1	11.6	13.0
Salary	13.8	14.6	16.0
Proportion married	87.0	89.1	87.2
Payroll			
Hourly (million of $)	184.4	143.9	99.9[b]
Salary	68.6	58.3	26.2[b]
Major assembler[c] rates ($/hr.)	9.11	10.22	10.25[d]
Vacation pay, hourly (millions of $)	13.2	15.8	12.5[b]
Retirees			
Hourly	2,026	2,317	2,482
Salary	925	985	1,130

a These figures are slightly different from those given in Table 2 (based on press reports), in part because the latter are for the full year rather than for a given month. In both cases, however, the same trends are evident.

b Through to the end of May 1983.

c Represent 27 per cent of the total hourly workforce.

d As of December 1983.

SOURCE: Data provided by Mr. W.J. Fisher, Director of Personnel Chrysler Canada, during personal visit 13 July 1983 and in correspondence 15 July 1983.

training have not been documented publicly. However, in September 1982 Lloyd Axworthy announced a retraining program at Chrysler.[27] Some $870,000 would be used to recall and retrain several hundred laid-off workers in new production methods in Windsor. Although the UAW and the NDP pressed the government for the reimplementation of the Transitional Assistance Benefits (TAB) program this has not occurred.[28] TAB was implemented originally by the Department of Industry, Trade and Commerce to compensate for jobs lost in 1965 when the Auto Pact was signed. Debate in the press focused on whether auto workers should receive any more special concessions, particularly since TAB was implemented to compensate for government trade policy, and problems in 1980 had little or nothing to do with that policy. In addition, more than half of the 22,000 unemployed in Windsor were not auto workers.[29] Lloyd Axworthy reasoned that 95 to 96 per cent of Windsor workers were covered by UIC and would qualify for extended benefits plus a $350 million adjustment program proposed by the Minister of Finance to provide assistance (e.g., early-retirement benefits) to workers in regions with industries in decline.[30]

Impact on dealers and suppliers

The potential impact of a Chrysler failure is evident from the fact that about 10,000 employees work for suppliers whose production is directly related to Chrysler, and that there were about 12,000 employed in Chrysler dealerships in 1982. These related groups are each roughly comparable to the size of the Chrysler workforce itself (Table 4). Although they would not necessarily be unemployed if Chrysler failed, and might regain employment within a short period, there would have been a substantial temporary impact while dealers and suppliers changed their orientations to other automobile companies or exited from the industry.

As part of the American loan-guarantee agreement, Chrysler Corporation (US) was required to gain matching concessions from its creditors. The new money invested by dealers and suppliers as a consequence of the American loan guarantee was invested at a reduced risk since the likelihood of Chrysler's failure was reduced by the willingness of the American government to come to the company's assistance. In 1980 many dealerships purchased $1,000 bonds sold by Chrysler Corporation Detroit in an effort to raise the funds necessary under the American

TABLE 4
Estimated provincial distribution of Chrysler employment, 1982

Province	Employees in dealerships	Employees in company
British Columia	1,000	51
Alberta	1,290	55
Saskatchewan	1,060	59
Manitoba	830	
Ontario	3,820	10,797
Quebec	3,000	157
Prince Edward Island		
Nova Scotia		
New Brunswick	1,000	56
Newfoundland		
All provinces	12,000	11,175

SOURCE: *Toronto Star* 30 June 1982.

loan-guarantee agreement.[31] Creditor concessions were not a condition of assistance to Chrysler Canada by the Canadian and Ontario governments.

Chrysler's Canadian dealerships were clearly interested in stalling the company's failure and willing to invest at a period of reduced risk. The impact of Chrysler's troubles had been such that in May 1980 the Toronto Auto Dealers Association reported that the number of Chrysler dealerships in Canada had fallen since 1978 from 635 to 618.[32] In February 1980 Chrysler Credit Corporation had placed the largest Chrysler dealer in Canada, Parkway County Chrysler of Toronto, in receivership.[33] Average assets, excluding inventory, of each dealership are approximately $1.1 million, rising to $3 million in urban areas, with an average employment of thirty persons.[34]

Chrysler suppliers purchased $78 million in debentures in Canada and the United States in the belief that a 'healthy Chrysler in the future will remember the help'.[35] In general, Canadian suppliers were willing to enter concessionary arrangements with Chrysler Canada, although these arrangements were less explicit than those negotiated between Chrysler Corporation (US) and its suppliers. The co-operation of Canadian suppliers was elicited in part, presumably because 75 per cent of

automotive-component suppliers are subsidiaries of American firms which build on demand from their parents.[36]

Robert Calder of Waterville Cellular, Quebec, which produces door seals for Chrysler K-cars, stated that he understood the risks entailed and would not cut Chrysler off when it stopped payments in December 1980. He suggested that 125 of his 400 employees would be laid off if Chrysler failed, although he was certain that this would not occur. A less supportive approach was taken by Tridon Ltd. of Burlington, Ontario which supplies hose clamps to Chrysler. This part of Tridon's operation represents twenty jobs and less than 10 per cent of the company's volume. An official stated that Chrysler would be cut off if Tridon were not paid.[37] Bendix Automotive of Windsor shut down, in part in reaction to Chrysler's difficulties in June 1980, after fifty years of operation, eliminating 491 jobs.[38] Bendix's Windsor division had supplied 85 per cent of all of Chrysler North America's power-brake systems, and Chrysler had purchased 30 per cent of Bendix's total production.[39] In April 1980 Hayes Dana of Hamilton, which produces frames and side-rails, indefinitely laid off 993 workers.[40]

Chrysler annually purchases approximately $500 million worth of supplies and raw materials in Canada from 3,000 companies.[41] Pat Lavelle, president of the Automotive Parts Manufacturers Association, stated that he was expecting layoffs of approximately 30 per cent of the 55,000 persons in the auto-parts workforce, as the industry declined.[42] As a spokesperson for the suppliers he stated that the government should help facilitate Chrysler's survival but that the assistance agreement must include stipulations for the sourcing of supplies in Canada.[43]

Although there were few opponents to assistance to Chrysler, as will be seen in the discussion of the decision-making process, there was an important recommendation against a bailout. An internal document prepared by the Ontario Ministry of the Treasury and Economics (and leaked to the press) suggested that Chrysler could not be saved.[44] The analysts did not believe Chrysler could generate adequate cash flow to convert to small cars, and the K-car alone would not provide an adequate financial base. Chrysler would have to sell 600,000 cars in the United States and 125,800 in Canada to break even. The report stated that the Japanese car makers, Ford, and GM could easily pick up Chrysler's market share. The report's contention was that saving jobs might bring only short-term relief. Chrysler could not be separated from consideration of the auto industry as a whole, which required long-term restruc-

turing; some analysts argued that refusing assistance to Chrysler could strengthen other auto manufacturers.

THE NEGOTIATION PROCESS

Chrysler Canada requested loan guarantees from the federal and Ontario governments on 11 August 1979.[45] President Lee Iacocca of Chrysler Corporation was then in the process of negotiating such guarantees with the American government, and Chrysler Canada president Don Lander was assigned the task of conducting the negotiations in Canada (he was replaced in July 1980 by M.J. Closs).[46] Chrysler Canada pointedly refused to use the term 'bailout', insisting that the company was requesting long-term financial and developmental help, not short-term rescue aid. In September 1979 Don Lander stated that Chrysler Canada did not need aid because it was still a strong third in the Canadian market.[47] Despite losses recorded since 1978, without aid the company would not face bankruptcy since the American and Canadian situations were different. Chrysler Canada was carrying smaller inventories, and its car sales had fallen only 4 percentage points below 1978 levels. Chrysler Corporation's share of the American market had also fallen by 4 percentage points to 7 per cent.[48] Chrysler's reluctance to admit its financial troubles could have reflected an attempt to retain consumer confidence and prevent a further fall in sales.

Key private-sector actors in the United Auto Workers Union were Douglas Fraser, the American president (until May 1983) and Robert White, the Canadian president. Douglas Fraser announced in early May of 1980 that Chrysler Corporation would go bankrupt if there was no agreement within a week.[49] Rank and file in Windsor, led by the local union president Frank LaSorda, expressed the workers' fear of a company failure. The UAW actively supported the bailout request. However, members exhibited a limited willingness to make wage and other concessions in contrast to their American counterparts who had been more co-operative and made concessions regarding paid holidays, wages, and benefits and the deferral of annual pension payments. Not until February 1981 was a wage cut accepted.[50] As discussed in more detail in the subsequent section on labour-relations issues, the Canadian UAW rejected the American request to forgo wage increases for two years in August 1979. Indeed, in September 1979 UAW Windsor had threatened strike action, despite Chrysler's problems, should talks fail concerning

demands for parity with Ford and GM workers.[51] In 1980 the attitude expressed by one worker was that the Canadian government had no choice but to help: 'We pay their taxes. They pay our unemployment insurance. If they want thousands of people out of work it'll cost them'.[52]

Members of the community were concerned with the potential ramifications of a Chrysler failure. Windsor mayor Bert Weeks stated that, 'if Chrysler goes down, so does a big part of Windsor'. He and Bob Richardson, general manager of the Windsor Chamber of Commerce, lobbied the media, Queen's Park, and Ottawa to encourage assistance to Chrysler. An overwhelming majority of editorials in Ontario newspapers supported the bailout.

Public-sector actors included Progressive Conservatives Michael Wilson (Minister of State for International Trade until February 1980 and then industry critic following the election of the Liberal party); Robert de Cotret (Minister of Industry, Trade and Commerce) who was replaced by Herb Gray who in turn was replaced by Ed Lumley in 1982; Mark MacGuigan (External Affairs) and Eugene Whelan (Agriculture). Gray, MacGuigan, and Whelan held the ridings of Windsor West, Windsor-Walkerville, and Essex-Windsor respectively. Active Opposition Members were Ed Broadbent, Bob Rae and Ian Deans (NDP industry critic) and Conservatives Otto Jelinek, Bill Kempling (Burlington), and Sinclair Stevens (York-Peel). Ontario was the affected provincial arena with Larry Grossman (Industry and Tourism), NDP leader Michael Cassidy, Liberal leader Stuart Smith, and Liberal MPP Robert Nixon (Brant-Oxford-Norfolk) as the active participants. Pressure also emanated from Washington, particularly from Treasury Secretary William Miller.

As a result of the federal election of 18 February 1980 in which the Liberal party regained power, the political actors played dual roles. Pre-election, the Liberal Opposition actively supported aid to Chrysler. Mark MacGuigan stated in the House that Chrysler's proposed investment package and corporate plan were positive for Canada, and that the country must take advantage of the opportunity to balance automotive trade with the United States.[53] Gray questioned why the Conservatives were waiting for the American decision since Congress was divided on the issue and positive action in Canada could tip the balance. If Chrysler US failed it would mean certain bankruptcy for Chrysler Canada.[54] The NDP also stated that it was necessary to act. If jobs were to be saved and research and development to occur in Canada

then the fact that Chrysler is a large American corporation should be viewed as an incidental matter.[55] No prominent political actor went on record against the bailout; there was a federal and provincial (Ontario) consensus that action was necessary.

The Clark government proceeded slowly, continually asserting, under repeated questioning in the House, that it would await the US decision.[56] The Canadian decision was delayed until after the election. During the campaign the Liberals pledged aid to Chrysler. Following the election there was limited serious opposition to the principle of aid. Pressure groups such as the UAW and the Automotive Parts Manufacturers Association favoured aid, with qualifications such as job guarantees and parts-sourcing stipulations. Opposition was expressed by the Canadian Federation of Small Business which stated that bailing out is 'throwing good money after bad' since Chrysler's troubles were due to its failure to meet consumer demand.[57]

American pressure on Ottawa to develop an aid package emanated from a number of quarters. In May 1980 when Fraser announced that Chrysler would fail without an agreement in a week, he added that one of the key elements in reaching an American agreement would be the Canadian decision. As part of the American package Chrysler had to raise $2 billion from the United Auto Workers, its suppliers, state and local governments and private sources. Herb Gray stated that Canada's refusal to help would have hurt the parent's ability to raise the $2 billion. In addition, Chrysler Canada is dependent on and integrated with its parent to the extent that failure to meet the requirements would have doomed Chrysler Canada. However, Larry Grossman asserted that Chrysler US did not need Canada's participation since it was required to raise only $250 million from state and local governments and this had been achieved before May 1980. A barrier to assistance from Ontario was Chrysler's refusal to give quantitative workforce guarantees. Nevertheless, on 8 May 1980 US Treasury Secretary William Miller called Herb Gray to urge that Canada act quickly or Chrysler would die by the end of the month.[58] The US Loan Guarantee Board was awaiting an announcement of Canada's intentions.

Due to this interdependent relationship between Chrysler Corporation (US) and Chrysler Canada, the auditors for Chrysler, Touche Ross Ltd., had to qualify Chrysler Canada's financial statements. In 1979, they gave an opinion which attested to the reliability of the financial statements subject to the ability of the parent company to get financing. By

1980, the auditors stated that they were 'unable to express an opinion' as to whether or not the financial statements fairly presented the company's financial state'. Since generally accepted accounting principles are applicable to a going concern, the auditors stated that the financial statements

> do not purport to give effect to adjustments, if any, that may be appropriate should the parent company and hence the company be required to sell the real assets and liquidate its liabilities, contingent obligations and commitments in other than the normal course of business and at amounts different from those in the financial statements.

Table 5 illustrates the dependent nature of Chrysler Canada relative to its parent company, Chrysler Corporation.

The assistance process had been initiated by Chrysler Canada on 11 August 1979 when it made a formal approach to Ottawa and Queen's Park. The secrecy of the negotiations was an important feature of the policy process. Although the Liberal government had publicly stated that it favoured aid to Chrysler, no concrete details of potential agreements were released until the decision was made. The stated rationale of this secrecy was the necessity of protecting Chrysler's competitive position. Another reason for the secrecy was the adverse affect on investor and consumer confidence if the details of Chrysler's financial situation were given wide publicity in the media.

Between August and December 1979 following de Cotret's statement that he was 'prepared to assist in any way considered acceptable by the federal government', the Conservative government carried out negotiations. Chrysler Canada's problems largely originated in the drop in US sales of large cars (due to the energy crisis). Eighty per cent of Canadian production is exported, and the expensive conversion of the Windsor V-8 engine plant to the production of a smaller, fuel-efficient, four-cylinder car had not yet been undertaken. In October 1979 it was announced that Chrysler Canada's modernization plans would be studied by fifteen officials from the federal Departments of Industry, Finance, Employment and Immigration, DREE, and Science and Technology.[59] Chrysler US had already begun the process of extensive reorganization.[60] On 19 December 1979 Congress announced a $1.5 billion loan guarantee. However,

TABLE 5
Vehicles and parts purchased by and from parent company, 1980, 1981

	1981	1980
Per cent of vehicles purchased by parent company	84	79
Per cent of vehicles purchased from parent company	81	83
Per cent of component parts supplied by parent	60	60

SOURCE: Chrysler Canada Financial Statements 1980 and 1981.

Prime Minister Joe Clark had been forced to call an election in Canada and had postponed the Canadian decision.

The new Liberal federal government opened talks with Chrysler in March 1980. Chrysler's original request was for approximately $750 million in loan guarantees in return for $1.2 billion in new investment in Canada over five years.[61] This was considered disproportionate to the $1.5 billion granted by the United States for $12 billion in new investment. Canada held a number of important levers which it used to scale down its commitment, one being the $243 million in outstanding duty payments (14.2 per cent duty on automobile imports) owed by Chrysler for inadequate production levels in 1980 under the Auto Pact.[62] The fact that these outstanding duty payments are, in effect, being ignored may be viewed as a form of assistance to Chrysler.

Gray's concern was in part with Canada's auto-parts deficit which had reached $41 million.[63] The bailout was to be used to balance Canada's problems with the Auto Pact by requiring more research and development, corporate decision-making, purchasing, and part-sourcing in Canada.[64] Gray's political determination to save Chrysler also had to be balanced with his strong nationalist stance which had become evident in other policy areas, such as his involvement in the creation of the Foreign Investment Review Agency. He refused Michael Wilson's demand that Chrysler negotiations be discussed before a committee of the House of Commons.[65] When Ian Deans qustioned Gray about his reaction to Lee Iacocca's public statement that there would be no job guarantees, no engine plant in Canada, and no small-size world car for production in Canada, Gray answered that he would negotiate job guarantees.[66] The Liberal government consistently refused to reveal the status of these negotiations.

THE LOAN-GUARANTEE AGREEMENT

On 10 May 1980 an Industry, Trade and Commerce release announced the details of the policy decision. On 13 May 1980 Gray made his statement to the House of Commons. At the heart of the negotiations had been the dispute over job guarantees. The UAW had been consulted during the talks and it, with the federal NDP and the Ontario government, had stood firm on the issue of quantitative job guarantees.

The Chrysler-federal government agreement consisted of guaranteed investment levels in Canada by Chrysler of $1 billion over five years from 1981 to 86 in return for $200 million in loans from private-sector financial institutions to be insured by the Canadian government. In 1980, Chrysler Canada restructured its bank debt which consisted of principal sums amounting to $188,300,000. The bank terms of the restructuring were to unconditionally forgive 2.5 per cent of the principal. In addition, 5.5 per cent was payable on a current basis and 7 per cent was deferred until 30 June 1984. Interest on the deferred portion was set at a 15 per cent annual rate. The deferred portion with compound interest would be repayable in twenty equal installments. After 30 June, all amounts outstanding would bear interest at an annual rate of 0.25 per cent above prime (Chrysler Financial Statements 1980).

This would help Chrysler to meet its investment program to convert plants to small cars and help finance the engineering and design costs of building new plants. In 1980, Chrysler Canada promised that the proceeds from the sale of any assets would be put into a trust account and used only for expenditures relating to front-wheel-drive compact cars and front-wheel-drive passenger cars. The retooling of the Windsor V-8 plant would cost $400 million, with $250 million to improve existing facilities and $300 million to expand existing assembly and manufacturing operations including the Etobicoke aluminum-casting plant.[67]

Chrysler Canada was to increase is autonomy with regard to purchasing, marketing, and production. The 1980 financial statements stated that trade accounts between the company and parent would be subject to certain specific conditions. In addition, no dividends could be paid without trustee approval. Greater efforts to source materials and components in Canada were required where Canadian suppliers were competitive. However, 75 per cent of companies which supply Chrysler in Canada are subsidiaries of American firms. Since they produce short

runs on a large number of product lines on demand from the parent, the achievement of competitive status is difficult.

The loan guarantees were to be available as of 1 January 1982 and were tied to new investment in Canada. Assistance was to be delayed until 1982 in the event that Chrysler failed in the interim or reneged on its investment obligations. This would provide security for the federal government, since Chrysler was expected to be on stronger ground by 1982. Loans received under the guarantees were to be repaid over a five-year period in quarterly instalments six months after the launching of the T115 van-wagon (which Canada has an exclusive worldwide mandate to produce until the loans are repaid), but not earlier than 30 June 1984. Ottawa also received the option to purchase 11.3 per cent of the number of warrants of Chrysler Corporation being made available to the US government on the same terms and conditions. An equity position in Chrysler was rejected.

In arriving at a policy decision Herb Gray stated that he had become intensely frustrated with the tactics of the Government of Ontario. In March, Grossman had stated that Ontario would contribute aid in return for a firm job commitment.[68] Ontario's concern was with jobs in Windsor not Chrysler's survival since it was willing to use its funds in alternate areas to provide jobs. Ontario continued to hold out for more jobs until at the last minute it accepted Chrysler's promise of a research and development centre in Windsor.[69] The Ontario government promised Chrysler a $10 million grant for its plastics and aluminum research centre,[70] as a contribution towards the estimated $20 million cost of building the facility in Windsor. If Chrysler were to fail, the centre would revert to Ontario ownership.

Chrysler agreed to maintain the ratio of Canadian to US jobs at 9 per cent for the first two years and 11 per cent thereafter and to reach a figure of 15,900 by 1984.[71] This level was subject to economic and market conditions.

Monitoring and reporting obligations by Chrysler included the submission of quarterly financial and sales reports, and the receipt by the Canadian government of all Chrysler reports to the US Loan Guarantee Board. Ottawa also received the right to appoint a director to the board of directors of Chrysler Canada Ltd. None of the facilities of Chrysler Canada were to be closed without the approval of the Minister of Industry, Trade and Commerce. Any 'deviation from the investment, financing, facilities, or products outlined in the plan or from the

proportional-employment commitments will occur only with the consent of the minister'.

There was criticism of the agreement in the House of Commons, although it was not extensive. Ian Deans questioned the strength of the job guarantees and of the provisions for research and development and Canadian parts sourcing. Gray stated that the Minister of ITC would decide if the agreement was being broken. (It is interesting to note that Chrysler announced a layoff of 1,400 within 48 hours of signing the agreement.) Concern was also voiced that Canada might not be producing the K-car on which Chrysler's future was based; instead Canada would produce the luxury Imperial.[72]

The first sign of difficulty with the agreement occurred in January 1981. Chrysler's deteriorating financial position stimulated rumours that it would apply for a further draw on the $1.5 billion loan guarantee ($800 million had already been drawn by Chrysler). Concurrently, the US Government was considering a further $400 million, but Chrysler would have to cut its investments abroad. Within a week Chrysler Detroit announced it would scale down the $1 billion investment program proposed for Canada to $600 million. Nevertheless, M.J. Closs, president of Chrysler Canada, stated that the Canadian loan guarantee of $200 million was still required. Gray announced that Canada would still adhere to the guarantee even though the trimmed investment plans for Canada would mean reduced employment levels – to 12,300 from the 15,900 forecast – which was in effect a violation of the agreement.[73]

Nevertheless, on 13 February 1981 a revised agreement was announced. Important revisions included a $150 million loan guarantee with another $50 million potentially available for significant additional projects to replace the original $200 million loan guarantee for loans from the private sector; new investment levels of $681 million which were down from $1 billion; the loan guarantees of $150 million were to be used for the van/wagon and the K-car program.[74] The terms for Ontario's $10 million grant for the research and development centre were changed to an interest-free loan.

The agreement attracted extensive criticism in the House from all parties. Otto Jelinek stated that it was in every way inferior to the May agreement in that it meant fewer jobs and a 50 per cent reduction in the number of small cars Chrysler would produce in Canada.[75] Members criticized the agreement on the grounds that it favoured large business

over small business and questioned the propriety of rescuing a foreign company.

The rapid increase in gasoline prices had induced Chrysler to consider offering diesel-engine options in its passenger cars (following the lead of GM and European and Japanese manufacturers). At the same time overcapacity in the K-car plants in the United States indicated that the proposed K-car plant in Windsor might not be justified. Another issue confronting Chrysler was securing ministerial approval to shut down the money-losing Windsor spring plant.[76] Negotiations on these and other issues came to a head with the announcement on 12 August 1982 of a new loan-guarantee package. Major revisions included investment levels of $821 million in Canada (up from $681 million) and the reallocation of the $200 million guarantee toward a new project. Fifty million was to go to a new diesel-engine project and $150 million to the T115 van/wagon. Some $12 million in repayable contributions would assist Chrysler in a joint venture with Perkins Engines (a Massey Ferguson subsidiary) to produce light diesel engines in Windsor's closed engine plant. The K-car would not be produced in Canada. Ontario would contribute an additional $33 million in loan guarantees towards the diesel venture,[77] as well as its $10 million interest-free loan for the research and development centre. The diesel venture was expected to create 1,000 jobs, and provide a research and development opportunity for Canada. On 24 December 1982 the diesel-engine plant was scrapped due to a 30 per cent slump in US consumer demand for diesel-powered cars, and Chrysler announced it would close the Windsor spring plant in July 1983.[78] Chrysler's inability to compete in all segments of the market meant that it had become extremely sensitive to demand changes. The strike by the Canadian UAW from 5 November to 22 December 1982 led to a considerable revenue loss for Chrysler and left even less room for error.

As a result of the scrapped diesel plant, and the threatened closure of the spring plant, the federal government reconsidered its position. In the House Ed Lumley, now Minister of Industry, Trade and Commerce, succeeding Herb Gray, stated that Chrysler had made the request to close the plant, but that he had said Chrysler must propose alternatives. Ottawa would be tough and hold Chrysler to the agreement or else Chrysler could not expect the government to keep its word.[79] However, he cautioned that if '. . . we should decide not to continue or to go ahead

with the government guarantees, perhaps all 10,000 jobs at Chrysler Canada would be in jeopardy'.[80]

The guarantees remained subject to renegotiation until it was evident that they were no longer necessary. Canadian leverage rested on both the outstanding duty requirements that resulted from Chrysler's failure to fulfill Auto Pact production requirements in 1980, and the importance to Chrysler of the Canadian market. The 1980 financial statements reported that the Canadian government would not impose a levy provided that the production deficiency was made up by the end of the 1985 model year. The 1981 financial statements reported that the level of truck production was adequate, but an additional deficiency in car production had occurred.

In March 1983 meetings between Chrysler and federal officials were postponed while awaiting the task force report on the auto industry[81] which was expected to propose a broader approach to the troubled industry. This has since been released, but Chrysler's return to profitability has meant that new negotiations are not required.

Labour-relations implications

Until 1982 Chrysler was the only major auto company to conduct international bargaining. Whenever collective bargaining took place a master agreement was negotiated for all Chrysler workers. Only local, nonmonetary issues were worked out at the plant level. This practice was established in 1967 and until the 'bailout' period it resulting in nominal wage parity for U.S. and Canadian workers. Wage parity also existed between the 'Big Three' auto companies until 1979. Industry-wide parity was a tradition and, as evidenced by the events of 1979 and 1982, attempts to change this met with considerable resistance.

In 1979 when the US Senate passed a resolution tying Chrysler aid to concessions from suppliers, dealers and employees, the American arm of the UAW agreed to reopen the newly signed collective agreement and take wage cuts to comply with the aid conditions. However, Robert White and the Canadian Chrysler members refused to entertain similar concessions, claiming that they would not be dictated to by the US government. Although the American members were outraged, particularly as this meant a greater wage cut for them,[82] White's stand gave credence to the position that Canadian members of international unions

had some independence from their American counterparts. The Canadian government never made employee concessions a condition for aid.

A second significant labour-relations incident occurred in late 1982. Throughout October and November of 1982 the UAW and Chrysler were engaged in acrimonious confrontations. The UAW insisted on closing the $3 per hour wage gap with GM and Ford. Iacocca and Closs maintained that Chrysler was not regularly profitable enough for wage parity, and that the $1 billion cash surplus was required as a credit line, and could not be used for wages. Iacocca stated that Chrysler had actually lost on automobile production in 1982; its profits were attributable to the sale of its tank division. If the UAW were to strike he claimed that Chrysler would be crippled.

In October 1982 bargaining in the United States stopped; an agreement was reached to reopen negotiations in January 1983. A strike vote had already been taken in Canada and senior union and management people from the United States were brought in to avert what was claimed to be a disaster for Chrysler. The union softened its stand somewhat by demanding wage increases but not necessarily parity.

Chrysler did not want to settle in Canada first, being reluctant to allow Canadians to set the pattern for the whole company. Robert White called for a return to Canadian collective bargaining. He also admitted that if they waited until January to strike the company would be able to stockpile the trim produced in Ajax (which was the strength of the strike threat).[83] Rumours began to circulate that Chrysler was retooling in the United States to pick up Canadian production.

The strike began in November. Bargaining began again in Detroit so that the Canadian strike could be settled. Although simultaneous bargaining occurred it soon became clear that a Canadian agreement would be the key to the US settlement. In December 1982, after a five-week strike, a settlement was reached giving the workers an additional $1.15 per hour, four COLA adjustments, improvements in the SUB plan and requiring no major concessions.[84] Interestingly enough, Ford workers (US) had reopened their contract with the company in February 1982, and agreed to concessions; Canadian Ford workers had refused to participate in either the negotiations or the settlement. GM and the UAW also signed an agreement in September 1982 providing for higher wage rates for Canadian employees relative to their US counterparts,[85] (although profit sharing in the latter case may affect this comparison).

A further labour-relations issue arose in July 1982 when Chrysler took a unique approach to its financial troubles.[86] The Windsor spring plant and other assets were offered to 330 workers in Windsor for $1 plus the value of a productive inventory priced at $2.3 million. Employees refused to purchase the plant in early August stating that Chrysler had a commitment under the proposed federal agreement to keep the plant open. In addition, they indicated that UAW policy does not favour 'picking up a company's dead wood'. The fate of the spring plant is uncertain, although it may be converted to produce mini-vans if high demand continues.

THE ECONOMIC AND POLITICAL IMPACT OF LOAN-GUARANTEE NEGOTIATIONS AND THE PROPOSED BAILOUT

Chrysler Canada has not called on its loan guarantees, nor utilized the grant from Ontario, nor has any agreement been finalized formally with Ottawa. Chrysler has made independent management decisions, and simply informed Ottawa of any new moves.

Chrysler Canada and Chrysler Corporation both returned to profitability in 1982. Employment levels at Chrysler Canada reached approximately 12,500 by 1984, well above the 1981 low of 9,225. In 1982, two of Canada's top-selling cars were produced by Chrysler Canada;[87] sales in 1983 increased by 61 per cent over 1982.[88] Chrysler's recovery has been partly led by the remarkable success of its T-115 mini-van for whose production the Windsor plant was retooled at a cost of $700 million. The plant is one of the most modern and efficient in the world, is equipped with robots, and operates on an efficient in-line sequence manufacturing basis. Chrysler dominates the mini-van market with only 20 per cent of total sales held by other firms, mainly Toyota.

In September 1983 Chrysler workers ratified a new contract which is to run until 15 October 1985. The agreement will allow Chrysler workers to recover within two years the parity with GM and Ford workers given up in wage concessions in 1981. The UAW has since attempted to reopen negotiations, in an attempt to recover more rapidly what was lost and to share in Chrysler's profits. Chrysler has refused to negotiate.

Chrysler's restructured finances, including the increased certainty created by the unused loan guarantee, increased productivity, and reduced costs led to the rapid recovery of market share from a low of 13.4 per cent in 1980, to 17 per cent in 1983.[89] Chrysler Canada recorded a

profit in 1983 of $78.8 million. By October 1984 Chrysler Canada had repaid its bank debts and negotiated a new $250 million credit facility with financial institutions, which indicates a restoration of confidence in the financial community.

Chrysler Canada's recovery has paralleled the recovery of Chrysler Corporation which recorded profits of $1.5 billion in the first six months of 1984[90] after moving into the black in 1982 for the first time since 1978. However, in 1982 the positive income statement was attributed to the sale of Chrysler's tank division, since the automotive division lost $156 million.[91] In May 1983 Lee Iacocca asked the US government not to cash in warrants to purchase 14.4 million Chrysler shares for $13 each. At the time of the loan guarantee Chrysler stock had traded at $4 per share, but had reached $28 by May 1983.[92] Thus, Washington was in a position to make a large profit. Iacocca resisted this and asked the US government to sell the warrants back to Chrysler because of his concern with the dilution effect of Washington's purchase. However, Iacocca retreated quickly in response to negative reactions from Washington, the public, and the media.[93] In August 1983 the US government announced that it would sell its warrants to the public through investment bankers. Chrysler Corporation has repaid the $1.2 billion US in US-government-guaranteed loans provided for in the firm's American bailout.[94]

It is generally conceded that the automotive industry must adapt to the continuing strength of foreign, and particularly Japanese, imports by increasing productivity and efficiency. Further measures have been proposed to aid the Canadian segment of the industry such as Canadian-content requirements,[95] and extended 'voluntary' import restraints.

NOTES

1 Chrysler Canada's stock is traded on Canadian exchanges, while Chrysler Corporation's stock is traded in the United States. There are two separate quotes for the parent and the subsidiary.

2 *Financial Post 500* 1979.

3 *Financial Post*, 17 October 1981. Chrysler Canada was the only North American automobile producer to gain ground against imports.

4 Chrysler's share of total Canadian Production (%):

1978	18.5[a]
1979	22.0[a]

1980 (May)	13.0[b]
	9.5[c]
1981 (January)	15.8[c]
1982	19.2[d]
1983	17.0[e]

a *Globe and Mail* 27 March 1979.
b *Financial Post* 28 September 1981.
c *Financial Post* 31 January 1981.
d *Financial Post Corp. Service* 4 May 1983.
e *Globe and Mail* 27 April 1983.

5 *Toronto Star* 26 February 1979. Chrysler US averaged an 11 per cent market share pre-1978 (*Time* 26 March 1983). Chrysler US market share reached a low of 8.8 per cent, but had risen to 10 per cent by November 1981.

6 *Financial Post* 31 January 1981.

7 These figures may not reflect a consistent trend since the different sources (as given in Table 2) refer to different seasons and sometimes to different concepts of employment.

8 *Montreal Gazette* 24 August 1979 – 12,000 of the 40,000 member manufacturing workforce in Windsor is employed by Chrysler.

9 Ibid., 31 January 1981.

10 *Montreal Gazette* 24 August 1979 Chrysler was pumping over $180 million a year into Windsor's economy.

11 *Globe and Mail* 27 August 1979.

12 *Toronto Star* 3 January 1980. William Purchase, manager of Sentry Department stores, stated that '. . . over Christmas there were a lot of layaways. People didn't have the money to buy things on the spot. There's a tense feeling in this city'.

13 Unemployment rate (%):

1983	16.9[a]
1982	–
1981	11.0[b]
1981	15.8[c]
1980	12.3[d]

a Stats Canada *The Labour Force* 1 April 1983.
b *Hansard* 4 November 1981.

c *Toronto Star* 4 July 1980 (Ontario average of 7.6%).
d *Hansard* 13 May 1980.
14 *Financial Post* 17 November 1979.
15 *Globe and Mail* 18 July 1980.

UIC Information Office (R.M. Schooley)
Registered Unemployed

June 1978	10,419
June 1979	12,486
June 1980	21,228

16 *Hansard* 13 May 1980.
17 *Toronto Star* July 1980.
18 *Financial Post* 31 January 1981.
19 *Toronto Star* 7 July 1980.
20 *London Free Press* 4 April 1980.
21 Ontario Ministry of Labour, reported week of 4 May 1983.
22 *Globe and Mail* 22 October 1982.
23 *Maclean's* 20 December 1982, 35.
24 *Globe and Mail* 18 July 1980.
25 *Toronto Star* 3 January 1980.
26 *Toronto Star* 23 June 1980.
Statistics produced by Windsor's unemployment office show that 200 leave Windsor every month, double the 1979 rate.
27 *Globe and Mail* 13 September 1982.
28 *Vancouver Sun* 25 June 1980 'UAW threatening demonstrations and sit-ins if the government does not provide relief such as TAB'. *Hansard* 8 May 1980 – Ed Broadbent, leader of the federal NDP pressed the government to reinstate TAB.
29 *Windsor Star* 18 September 1980.
30 *Hansard* 11 June 1980 and 8 December 1980. In July 1980, 986 jobless had their UIC expire. Of these, 574 were laid-off auto workers, 412 were others. Of the 574 laid-off auto workers, 456 had their benefits extended another forty-two weeks. Of the 412 'others' only 187 had their benefits extended.
31 *Financial Post* 31 January 1981.
32 *Toronto Star* 17 May 1980.
33 *Globe and Mail* 25 February 1980.
34 *Financial Post* 31 January 1981.

35 Ibid.
36 *Hansard* 13 May 1980 (Bill Kempling, MPP Burlington).
37 *Financial Post* 31 January 1981.
38 *Toronto Star* 23 June 1980.
39 Ibid., 11 August 1979.
40 *Hamilton Spectator* 19 April 1980.
41 *Financial Post* 29 March 1980.
42 *Toronto Star* 11 August 1979.
43 *Financial Times Canada* 1 October 1979.
44 *Financial Post* 31 January 1981.
45 *Toronto Star* 25 August 1979.
46 Ibid., 8 July 1980.
47 *Montreal Gazette* 7 September 1979.
48 *Globe and Mail* 7 September 1979. Chrysler US lost $1.1 billion on sales of $126 million in 1979 which is a loss of 9 per cent of sales. Chrysler Canada lost $31 million on $2.9 billion of sales, on 1 per cent.
49 *Hansard* 6 May 1980 – Michael Wilson.
50 *Toronto Star* 5 February 1981. The UAW accepted a twenty-one month wage freeze which would cost Chrysler workers $70 per week in lost wages and fringe benefits. The concessions were calculated to save Chrysler $150 million. *Globe and Mail* 13 February 1981.
51 *Globe and Mail* 24 September 1979.
52 *Toronto Star* 3 January 1980.
53 *Hansard* 15 November 1979 – Mark MacGuigan, Liberal.
54 Ibid., 5 December 1979 – Herb Gray, Liberal.
55 Ibid., 5 December 1979 – Ed Broadbent, NDP and 4 December 1979 – Robert Rae, NDP.
56 Ibid., 4, 6, 7 December 1979.
57 *Globe and Mail* 13 May 1980.
58 Ibid.
59 *Financial Times Canada* 1 October 1979.
60 *Time Magazine* 21 March 1983. Lee Iacocca's moves to save Chrysler had been

   1 to keep the K-car chassis and turn it into several models in efficient, large-scale production;
   2 new management – personnel was imported from Ford;
   3 cut inventory – end to 'sales bank' speculation practices;
   4 an aggressive ad campaign;

5 to cut the number of different parts used from 70,000 to 40,000; and

6 sold European assets and tank division.

This resulted in halving the break-even point for car production. The K-car, introduced in October 1980, had achieved 20 per cent of the compact car market within one year.

61 *Globe and Mail* 1 April 1980.

62 *Toronto Star* 15 February 1981.

63 *Hansard* 18 January 1983.

64 *Financial Post* 29 March 1980.

65 *Hansard* 25 April 1980.

66 Ibid., 1 May 1980.

67 Industry, Trade and Commerce News Release 10 May 1980:

Investment Proposals ($ million)

1980	1981	1982	1983	1984	1985
62	69	263	469	55	91

$413 million on T115 van/wagon 1982-1983
$161 million on new front-wheel-drive car 1982-1983
$177 million on improvements to manufacturing processes '82-'83
$40 million on modernizing Etobicoke plant 1981-82, 1985.

68 *Globe and Mail* 20 March 1980.

69 *Ontario Hansard* 12 May 1980.

70 *Financial Post* 24 May 1980.

71 Industry, Trade and Commerce News Release 10 May 1980.

Average annual employment levels:

1981	9,800	– 9% of US employment
1982	10,100	no less than 11%
1983	11,300	of US employment
1984	15,900	

72 *Hansard* 13 May 1980 – Herb Gray, Ian Deans, and John Crosbie.

73 *Globe and Mail* 6 January, 13 January, and 17 January 1981.

74 Specific details of the Restructured Agreement of 13 February 1981, include

a transfer of all remaining rear-wheel-drive production to the Windsor car-assembly plant in 1981.
b replacement of this arrangement in 1983 by the introduction of a new T115 van/wagon to be produced in Windsor.
c movement of the production of rear-wheel-drive vans and wagons from the Pillette Road Van Assembly Plant to the United States in 1984 (this was changed in the August 1982 agreement such that production remained in Canada).
d replacement of the van by the K-Car (Canada retained the van and the K-Car is to be produced only in the United States).
e maintenance of minimum average-employment levels at Chrysler Canada in relation to Chrysler Corporation 9 per cent in 1980-81, 11 per cent 1982-86.
f increased efforts to source materials, components, and services in Canada – increase Canadian research and development activity and greater autonomy of Canadian operations.
g facilities cannot be closed without the prior approval of the Minister of Industry, Trade and Commerce.

75 *Hansard* 18 February 1981.
76 *Globe and Mail* 7 August 1982.
77 Industry, Trade and Commerce News Release 12 August 1982.
78 *Globe and Mail* 27 December 1982.
79 *Hansard* 18 January 1983 – the Honourable Sinclair Stevens to Ed Lumley (Minister of ITC).
80 *Hansard* 21 January 1983 – Ed Lumley.
81 *Globe and Mail* 5 April 1983.
82 *Toronto Star* 3 January 1980. Specifically the Canadian UAW rejection of the pay and meant that each of Chrysler's American unionized employees was required to give up $4,400 instead of the $2,000 planned if the Canadians had joined in.
83 *Globe and Mail* 4 November, 10 November 1982.
84 Ibid., 1 December, 13 December 1982. The new assembler rate would rise from $9.07 to $10.22 per hour, including COLA.
85 Ibid., 20 September 1982.
86 Ibid., 2 July and 7 August 1982.
87 *Financial Post* 11 December 1982.

88 *Globe and Mail* 4 February 1984.
89 Ibid., 17 September 1984.
90 *Toronto Star* 3 August 1984.
91 *Maclean's* 15 November 1982.
92 *Toronto Star* 13 May 1983.
93 *Economist* (London) 16 July 1983.
94 *Globe and Mail* 2 August, 13 August 1983.
95 Ibid., 11 May 1983 – quotes report of the federal task force on the auto industry.

2
Massey Ferguson

INTRODUCTION

Massey Ferguson is a multinational manufacturer of agricultural machinery and diesel engines. Its extensive worldwide manufacturing operations are spread throughout thirty-one countries. Massey was formed 140 years ago in Newcastle, Ontario. During its early years, Massey developed its manufacturing capability by acquiring the rights to American patents. In 1891 Massey merged with the Harris Company (a competitor) to become Massey-Harris. In 1910, Massey opened its first US plant in New York state. Massey barely avoided bankruptcy in the 1930s. It posted losses of $2.25 million in 1930, $4 million in 1931, $3.8 million in 1932, $3.3 million in 1933, $2.2 in 1934 and $1.4 million in 1935. But its banker, the Canadian Imperial Bank of Commerce, kept the company going by extending its loans during these years. The Second World War brought relief for Massey-Harris, which had suffered a gradual decline during the 30s. The war turned the company around and, by 1945 sales were $116 million, of which $68 million came from war requirements production.[1] In 1953, Massey-Harris merged with Ferguson, a British tractor-manufacturing facility. By doing so it acquired competitive strength in Europe and particularly in Britain. In 1959, Massey Ferguson acquired Standard Tractor to increase the size and specialization of its manufacturing operations. In the same year Massey acquired Perkins Diesel, makers of industrial engines and engines for transport.

Argus Corporation, a large Canadian holding company, bought its first Massey shares in 1943. By 1960, Argus held 12 per cent of Massey

shares. From 1960 to 1965 Massey sales advanced at an average annual rate of 11.6 per cent and earnings grew 30 per cent. The company experienced financial problems in 1970 and 1971 but it continued to expand operations. By 1976, the company had 68,000 employees, sales of $2.8 billion and a record profit of $108 million.[2] This was the high point in the company's performance. In August 1978, Conrad Black, the new chairman of Argus, took over as chairman of Massey and attempted to improve Massey's profitability through rigorous cost-cutting measures and the introduction of new management.

The firm had maintained a solid reputation for innovative technology and superior engineering. Moreover, Massey was the first large Canadian manufacturer to achieve significant success in export markets. In 1980, Massey held 17 per cent of the worldwide market for tractors and 14 per cent of the market for combines. The firm has often been cited by Canadian business and political leaders as an exemplar of home-grown entrepreneurial success.

This case study explains Massey's recent decline and the efforts by its creditors and the government to prolong its life and nurse it back to health. The discussion begins with a brief description of the international market for agricultural machinery and implements, and the causes of Massey's difficulties. The narrative then shifts to the negotiations between Massey, its creditors, and both levels of government that resulted in Massey's rescue. The firm's performance and future prospects are then discussed in an effort to assess the consequences of the public and private arrangements designed to preserve Massey as a going concern.

BACKGROUND

The agricultural-implements industry

The agricultural-machinery business is a demanding one. Swings in company profits are not uncommon because the industry is so vulnerable to the boom and bust cycles that characterize farm-products markets around the world. As mentioned earlier, severe sales declines occurred in the 1920s, 1930s, and 1950s. In 1980, sales plummetted again, particularly in the North American market. President Carter's grain embargo, a drought in the midwest, and increased borrowing costs resulted in a dramatic reduction in North American sales. There was also a downturn in South American sales. A substantial share of Massey's

problems stemmed from this industry decline. In addition, the adverse publicity that flows from the possibility of bankruptcy damaged Massey's sales. The suggestion of bankruptcy decreases sales since consumers become concerned about resale value, the satisfaction of future warranty claims, and the availability of parts.

In the large North American farm-equipment market, Massey has traditionally ranked third behind John Deere and International Harvester. However, in 1980, it held first and second position in the markets for small (30-90 hp) tractors and in combine harvesters. Massey's weakness in North America was partly attributable to the fact that it lagged behind other firms in the development of large high-horsepower (90-324 hp) tractors. Massey introduced its first line of large tractors in North America in 1978.[3] The North American market for farm-machinery implements is characterized by virtually duty-free trade. Many North American firms have factories both in Canada and in the United States.

Massey's decline in the mid-seventies

Massey sales were volatile from 1978 to 1980. Statistics from the 1983 financial statements (see Table 6) illustrate this sales pattern. The 1980 sales would have been lower than reported but a change in accounting methods resulted in a higher sales figure. In 1980 Massey adopted the commonly used method of recognizing North American sales when products moved from the manufacturer's warehouse. Prior to 1980 Massey had recognized sales at the retail level, i.e., when they moved from the dealer's warehouse.[4]

Calculations derived from Massey Ferguson's financial statement (see Table 7) illustrate Massey's deterioration prior to the bailout. The current ratio for 1978 through 1980 is very low and the quick ratio (which excludes inventory from the asset calculation) shows that, in the event of liquidation, current assets were not sufficient to cover current liabilities. Prior to the bailout in 1981 the negative scores signal a prediction of bankruptcy for the company. (One year after the bailout the same signal is observed.) Massey's earnings performance is also quite poor. The Dupont method for calculating return on investment indicates that the low return on assets is due to poor profitability (ratio 7) and a deterioration in asset turnover (ratio 8).

TABLE 6

Massey Ferguson: financial statistics (millions of US dollars)

	Year ended 31 Jan. 1984	Three months ended 31 Jan. 1983[c]	Years ended 31 October							
			1982	1981	1980	1979	1978	1977[a]	1976[a]	1975[a]
Summary of operations										
Net sales	1,535	313	2,058	2,646	3,132	2,973	2,631	2,861	2,774	2,554
Gross profit	284	10	250	313	556	573	512	608	533	511
Net expenses (excluding interest)	253	65	317	263	520	392	467	431	281	280
Interest expense (net)	90	43	186	265	240	149	141	142	97	91
Provision for unusual costs and reorganization expense	16	–	171	5	29	95	73	–	–	–
Income tax recovery (expense)	1	2	3	9	10	6	(17)	(17)	(57)	(49)
Income from finance subsidiaries and associate companies	6	2	8	16	23	21	19	14	10	9
(Loss) profit from continuing operations	(68)	(94)	(413)	(195)	(200)	(36)	(167)	32	108	100
Loss from discontinued operations	–	–	–	–	(25)	(23)	(95)	–	–	–
(Loss) profit before extraordinary item	(68)	(94)	(413)	(195)	(225)	(59)	(262)	32	108	100
Extraordinary item	–	–	–	–	–	95	–	–	–	–
Net (loss) income	(68)	(94)	(413)	(195)	(225)	37	(262)	32	108	100
Operating (loss) profit[b]	(48)	(85)	(205)	(218)	(120)	45	(119)	78	130	119
Dividends										
Common	–	–	–	–	–	–	4	19	18	13
Preferred	–	–	16	45	–	–	2	10	7	2
(Loss) income retained	(68)	(94)	(429)	(240)	(225)	37	(268)	3	83	85

TABLE 6 (continued)

	Year ended 31 Jan. 1984	Three months ended 31 Jan. 1983[c]	Years ended 31 October							
			1982	1981	1980	1979	1978	1977[a]	1976[a]	1975[a]
Financial condition										
Working capital	556	670	723	994	256	467	476	736	767	666
Additions to fixed assets	36	5	47	44	46	77	99	147	175	170
Depreciation and amortization	37	14	71	81	80	88	77	69	54	45
Total assets	1,581	1,844	2,069	2,503	2,828	2,745	2,573	2,620	2,323	2,015
Current ratio	2.0	2.1	2.0	2.2	1.1	1.3	1.4	1.7	1.9	1.8
Asset turnover ratio	0.97	0.17	1.0	1.1	1.1	1.1	1.0	1.1	1.2	1.3
Debt/equity ratio	2.8	7.8	5.0	2.1	4.6	2.1	2.1	1.2	0.9	1.0
As a per cent of sales										
Cost of goods sold, at average exchange rates	81.5	89.8	83.0	82.1	82.0	80.1	81.1	78.2	76.8	77.6
Effect of foreign currency exchange rate changes	–	7.0	4.9	6.1	0.2	0.6	(0.6)	0.5	4.0	2.4
Gross margin	18.5	3.2	12.1	11.8	17.7	19.3	19.5	21.3	19.2	20.0
Marketing, general and administrative	14.2	22.6	16.8	15.6	12.9	11.8	12.6	11.9	11.5	10.6
Engineering and product development	2.3	3.0	2.3	2.2	1.9	2.0	2.2	2.4	2.2	2.2
(Loss) profit before items shown below	(3.8)	(31.3)	(12.3)	(8.1)	(6.5)	1.1	(3.7)	1.2	5.6	5.5
Provision for unusual costs and reorganization expense	1.0	–	8.3	0.2	0.9	3.2	2.8	–	–	–
Net (loss) income	(4.4)	(30.1)	(20.1)	(7.4)	(7.2)	1.2	(10.0)	1.1	3.9	3.9
Operating (loss) profit[b]	(3.1)	(27.1)	(10.0)	(8.2)	(3.8)	1.5	(4.5)	2.7	4.7	4.7

TABLE 6 (continued)

	Year ended 31 Jan. 1984	Three months ended 31 Jan. 1983[c]	Years ended 31 October							
			1982	1981	1980	1979	1978	1977[a]	1976[a]	1975[a]
Shareholders/employees										
Shareholders										
Common shares	30,912	31,871	32,961	34,897	28,351	29,926	31,353	30,619	31,039	35,844
Preferred shares	5,025	6,568	6,934	7,918	9,669	10,613	11,370	10,208	10,620	5,046
Employees (at year end)	27,609	30,095	33,726	39,789	41,690	56,233	57,983	67,151	68,200	64,572
Common shares outstanding (000s)	91,674	57,389	56,551	43,025	18,250	18,250	18,250	18,250	18,250	18,250
Preferred shares outstanding (000s)	21,136	21,136	21,136	17,463	3,825	3,825	3,825	3,999	3,999	1,600

a Results for 1980, 1979, and 1978 include the construction-machinery business as discontinued operation. It is not practicable to segregate the construction-machinery operation for years prior to 1978.

b Operating (loss) profit is defined as total revenue less those recurring expenses which are within the control of management. It excludes extraordinary items, net exchange, and reorganization expense pertaining to continuing operations.

c In certain instances, three-month data is not comparable to the summary of yearly statistical data.

SOURCE: Massey Ferguson Limited annual reports 1983 and 1982.

TABLE 7
Financial ratios: Massey Ferguson Limited

		1983[a]	1982	1981	1980	1979	1978
1.	Current ratio	1.99	1.97	2.18	1.11	1.28	1.34
2.	Quick ratio	1.13	1.13	1.29	.59	.56	.49
3.	Z score	1.01	(.56)	.83	(.98)	(.15)	(.74)
4.	EBIT/(interest and preferred dividend .5)	.22	(1.23)	.23	.22	1.13	(.07)
5.	EBIT/average total assets	.02	(.10)	.02	.02	.05	(.01)
6.	Net income/sales	(.04)	(.20)	.07	(.07)	.01	(.09)
7.	Sales/average total assets	.90	.90	.99	1.12	1.12	1.14
8.	(6)(7) = Dupon ROA	(.04)	(.18)	.07	(.08)	.01	(.10)
9.	Debt/(common and preferred)	2.29	4.33	1.81	1.59	1.08	1.21
10.	(Debt and preferred)/ common	(6.56)	(6.79)	7.37	2.56	1.49	1.68

a Year end changed from October to January.

Massey's financial difficulties are partially attributable to a chronic problem with operating costs. A review of its financial statements shows that the firm's cost of goods sold as a percentage of sales was generally increasing over the five-year period prior to its recent problems. As a basis for comparison, Massey's figures for cost of goods sold for 1980 indicated that its costs were 85 per cent of gross revenues; John Deere, a direct competitor of equivalent asset size and sophistication, reported cost of goods sold at only 75 per cent of its gross revenues.[5] Conrad Black observed that 'Massey Ferguson had approximately 78 per cent of the sales of John Deere and Co. and had approximately 115 per cent of Deere's number of employees.'[6]

In addition to its cost-control difficulties, Massey's gross profits were further eroded by an unexpected increase in the value of the British pound. Perkin's Diesel was exporting 86 per cent of its production in 1980. Sixty-eight per cent of these exports went to Massey Ferguson.[7] Finally, Massey's high short-term debt-to-equity ratio rendered it extremely vulnerable to the unprecedented increases in interest rates that occurred in 1979-80 because the debt was at a floating rate. The firm's interest expense had increased 58 per cent from 1979 to 1980! Massey's current bank loans were up 98 per cent from 1979 and

represented 41 per cent of total debt. The current portion of long-term debt was $60.2 million. Accounts payable were 16 per cent of total debt. Accounts payable usually are composed mostly of supplier accounts. (One writer reported that, in the summer of 1981, suppliers had to call Massey for payment to meet their own payroll obligations.)[8] Table 8 shows the employment and dollar impact of a Massey shutdown. the Industry, Trade and Commerce figures show that 3,000 Canadian jobs related to the supplying of Massey parts would be lost if Massey closed down and the annual dollar impact would be $125 million.

Massey had $4.26 worth of debt for every dollar's worth of equity compared to the debt figures of $1.40 for International Harvester and $1.10 for John Deere.[9] Massey's poor performance not only increased the risk of default for the creditors but shareholders also saw their equity position deteriorate. Massey's common-stock prices actually went from a 1976 high of $32.00 per share to a 1980 pre-bailout low of $5.75. Argus president Conrad Black responded to this equity erosion by divesting Massey holdings; in October 1980 Argus gave its 3 million shares of Massey to Massey's pension funds. The Argus divestiture was ostensibly to clear the way for the government to become involved in a Massey bailout. However, Argus also took a $39 million tax write-off when it gave the shares to the Massey pension funds. The tax treatment is now being reassessed by the Department of National Revenue which has questioned whether the Argus shareholders are entitled to the tax write-off.

Massey's bank creditors

Most of Massey's debt was held by investment bankers distributed around the world. The breakdown of major debt holders prior to the bail-out was: Canadian Imperial Bank of Commerce (CIBC) – $360 million, British banks – $415 million, US banks – $915 million, and French banks – $170 million. Additional loans were held by bankers in Switzerland, Italy, Germany, Australia, and South America. Two other Canadian banks had very small claims against Massey – the Royal Bank and the Toronto Dominion Bank.[10] The amount of bank exposure varied. Some banks – the Canadian Imperial Bank of Commerce, for instance – could have lost a lot. Regarding CIBC security, Conrad Black stated 'if worse comes to worst, I think you'd find the Commerce the proud owner of Massey's Brantford Ontario plant.'[11] Other banks, including some in

the United States had spread out their debts so that the Massey debt exposure for any one bank was not so great. On the other hand, the British banks would be severely criticized by government and labour for pulling the plug on Massey. The number of British workers involved (17,000) and the regional distributions of these workers would make a Massey closure very controversial.

The CIBC financial statements prior to 1981 did not state the actual amount of its exposure in Massey Ferguson. In the bank's 1981 financial statements, Massey's problems are discussed only as they related to a $100 million write-off of Massey's debt. Roy Palmer, bank analyst with Alfred Bunting and Company, says the uncertainty about the Massey exposure was a contributing factor to the CIBC's low price-earnings ratio relative to other banks on the market.[12]

Some of the most intense pressure on the federal government during the period preceding the bailout was being applied by the banking community. The CIBC's recoverable security was estimated at less than half the value of Massey debt. In addition, the lost interest revenue would have an immediate adverse effect on CIBC profits.[13] Analysts' opinions differed the effect of a Massey writedown. One analyst stated that if $310 million in loans had to be written off CIBC bank profit would fall by $1.30 a share.[14] (In 1979, the CIBC earned $5.14 a share.) Another analyst reported that a $100 million write-off in addition to lost interest would reduce CIBC earnings by 70 cents a share.[15]

Most of the banks expressed a strong desire to avoid putting Massey through bankruptcy proceedings. Bankruptcy litigation was likely to be protracted because Massey's assets were distributed across many nations and collection procedures would have to be initiated in each of the jurisdictions. Several experts observed that legal proceedings could last anywhere from five to ten years. With rapid inflation and the interest revenue lost during the bankruptcy proceeding, the banks could have expected to suffer heavy losses. The multinational nature of Massey's operations complicated negotiations because creditors in different countries held disparate bargaining positions. The creditors located in those jurisdictions where the bulk of Massey's assets were located were more likely to recover their claims. Other bankers in jurisdictions with relatively advantageous collection procedures would be likely to hold out for a better deal. One feature of the bailout negotiations was the legal manoeuvres initiated by banks to restrict the transfer of Massey assets

from one country to another so there would be more assets available in the event of bankruptcy.

The banks were not the only potential claimants if Massey were forced into bankruptcy. An Ontario Task Force reported in November 1981 that 30 per cent of farm-machinery dealers would go out of business within the next six months.[16] September tractor sales in 1982 were down 33 per cent from the previous year's already depressed sales. As Table 8 shows, ITC estimated that 6,000 Canadian jobs related to the farm-machinery dealer network would be lost if Massey went bankrupt.

A full or partial closure of Massey's operations would also eliminate jobs in many countries. The plant closures would, moreover, generate more severe adverse impacts for particular regions and communities. In the case of Canada, Brantford would be hardest hit in the event of a Massey failure since Massey is the city's largest employer. Brantford's other major employer is White Farm Equipment Company. This firm has received substantial federal and provincial assistance including direct grants from the Ontario government and loan guarantees from the federal Enterprise Development Board.

Massey's first major Canadian layoff stretched over three months in 1980. In August the company laid off 5,000 Canadian workers, 3,240 in Brantford and 1,848 in its Toronto operations. At the same time, White had also laid off 1,000 hourly workers. The total lost wages in Brantford over the three-month period was estimated at $18 million. The *Toronto Star* reported that 15,000 jobs in the area were affected by the two plant closings.[17] The supplementary-benefits fund, which had been negotiated by the employee's union, the United Auto Workers, stood at $2.5 million at the time of the first layoff. With 5,000 workers laid off, the supplementary benefits pay could only last three weeks.[18] (The company figures showed that there was only $1.1 million in the supplementary-benefits fund and that only seventy-one workers were eligible; supplementary-benefits pay could last twelve weeks and only 14 per cent of the workers were eligible.)

The Brantford and District Labour Council reported that there were 5,800 workers seeking work in 1979 through Canada Manpower. By 1981, there were 7,200 seeking work, and, by December 1981, 8,000 Brantford area workers had registered with Canada Manpower. In 1981 Brantford reported that unemployment levels had reached 25 per cent in manufacturing and 30 per cent in construction. The effect of these high levels of unemployment was a doubling of social-service budgets over a

TABLE 8
2 September 1980 ITC evaluation of impact within Canada of Massey Ferguson shutdown

	Employment	C $ million
Massey Ferguson manufacturing		
Operations	6,500	500
Suppliers	3,000	125
Farming community (50% depreciation)		
Dealerships	6,000	230
Balance of trade		600-700
Opportunity loss (Diesel-engine plant)	12,700	
Loss to financial community (Banks and shareholders)		535
Balance of trade loss		
Loss of exports	C$425 million	
Import substitution	C$300 million	
TOTAL	C$725 million	

SOURCE: Industry, Trade and Commerce.

two-year period. In 1979, the monthly caseload for Brantford County Social Service was 743 residents. In 1979, the cost of these services was $2.2 million. By 1981, the caseload had increased to 1,100 residents at a cost of $3.8 million. The incidence of suicides, divorces, and wife and child-beating had increased during this period and a Brantford resident faced a three-week waiting list to receive help in coping with these problems. The projected social-services costs for 1982 were $5.8 million.[19] The *Toronto Star* reported that Larry Grossman, then the Ontario Minister of Industry and Tourism, was working hard to get an Industry and Labour Adjustment Program (ILAP) grant for Brantford from the federal government. The ILAP grant would provide some relief, but by the beginning of 1981 a crisis was looming for Massey and Brantford and an immediate solution was necessary.

The Ontario debate

While the economic environment in Brantford was deteriorating, the UAW, which represented Massey's North American hourly workers, was pressing for government action to protect Massey's employees. At the provincial level, the Ontario Federation of Labour held a rally at Queen's Park. Robert White, head of the UAW, called for direct relief for labour in the form of: portability of pensions; one week of severance pay for each year of work; and six-months notice of permanent shutdown. Mr. White argued that such measures were necessary to deter plant closings and ensure some relief for workers. The NDP and Liberals, at the same time, supported a bill in the Ontario legislature that would ensure employer contributions to benefits during the layoff notice period. It would also provide eight-weeks notice for firms employing up to 200 workers, twelve-weeks notice for firms with 200 to 500 workers and sixteen-weeks notice for firms with more than 500 workers.[20]

Aid to Massey was not a foregone conclusion, although all parties expressed a commitment to the necessity of maintaining employment in Brantford. Larry Grossman, Minister of Industry and Tourism, stated that Ontario was talking to both Ottawa and Massey. An injection of funds would not be enough for long-term survival – the main concern must be jobs.[21] Robert Nixon, MPP and Liberal leader stated that Massey might go bankrupt if it did not meet the test of its creditors at the end of October. The farmers were losing confidence in Massey's ability to service its machinery.[22] Opponents of Massey aid said that government funds should not pay for Massey's mismanagement, particularly mismanagement of debt. Nixon stated that he had conversations with Massey employees who felt Massey should not receive aid since its management decisions and administration were incompetent.[23] The federal government's immediate response to the problem was to provide an extension of unemployment-insurance benefits for all unemployed workers entitling them to benefits for up to fifty-two weeks instead of the regular twenty-six weeks. Later, they would give more direct aid to Brantford in the form of the ILAP grant. (This program provides interest-free loans to cover 50 per cent of capital-cost expenditures for existing or new businesses in a region.)

The federal debate

There was limited discussion of the Massey Ferguson situation in the federal arena. Debate centred on the issues of employment, the decline of the farm-machinery industry and Massey's ties to foreign and Canadian banks.

In May 1980 Derek Blackburn MP asked Herb Gray why Massey was laying off 5,000 workers in Brantford and closing from August to October.[24] Gray replied that sales of tractors to the United States in the industry were down 40 per cent, and sales of combines were down 45 per cent, and thus Massey had to deplete its inventory. Ian Deans (NDP House Leader) noted in December 1980 that the net real income of farmers was in decline and the market for farm machinery was anticipated to be $2,068 billion for 1981.[25] If Massey Ferguson were to fail then these farmers might be forced to seek imported machinery which would be more expensive. He made no mention of Canadian-based alternatives, such as John Deere.

Michael Wilson, (PC industry critic and a Toronto area MP) charged that aid to Massey might be perceived as support for, or a bailout of, Argus Corporation.[26] Conservative MP Elmer Mackay claimed that Massey's Canadian operations in relation to its worldwide activities were negligible.[27] He expressed concern that Massey not be permitted to use bailout funds to settle its debts around the world. There was a general concern that Massey make firm commitments on investment, production, and research and development before it received any aid commitment.

Ed Broadbent (NDP leader and an MP from Oshawa) noted that Massey's principal investors, or largest shareholders, were its employees through the pension funds.[28] He questioned whether the government should be granting guarantees to new private investors so they would not face risks, while workers whose pension funds were tied up in Massey would not be backed. He charged that an infusion of new capital would mean that shares already held by workers would drop in value through dilution. Herb Gray (Minister of Industry, Trade and Commerce) replied that if Massey Ferguson were to fail the pension funds would be worth nothing. New equity would have to be attracted to enable adequate refinancing.

NDP MP David Orlikow questioned how J.D. Leitch, who was on the board of directors of both Massey and the CIBC, could be expected to protect CIBC depositors and make loans to Massey.[29] Quoting the *Globe*

and Mail (unnamed date) he stated that the CIBC and Massey shared board directors. Ian Deans noted that British, French, German and Italian banks had sought and attained assurances from Massey that it would continue to invest heavily in their countries.[30] He questioned whether their governments had made guarantees. Gray replied that Britain would guarantee $90 million in preferred shares which British banks would take in lieu of the debt owed them by Massey.

The bailout

On 20 October 1980 the governments of Canada and Ontario announced they had reached a compromise, in principle, with Massey and its lenders. *The Wall Street Journal* stated that:

> The governments are prepared to guarantee the capital risk of a portion of the new equity investment in Massey, providing various conditions are met, including a satisfactory degree of cooperation from the existing lenders.[31]

The primary agreement between Massey's bank creditors was arranged on 16 January 1981. The banks agreed on an equal-treatment-for-all interest-forgiveness scheme, according to which each bank was obligated to forgive interest to 22.5 per cent of the principal amount of its loans to Massey. In return, the banks took Massey common shares worth $275 million allocated in proportion to their relative shares of Massey indebtedness. Moreover, all the banks agreed not to reduce the credit extended to Massey from current levels for at least three years, and in the fourth and subsequent years, not to withdraw more than 25 per cent of their outstanding credit in any one year. In addition, Massey was able to raise $90 million from the sale of preferred shares to the public; these shares were guaranteed for their par value by Britain's Export Credit Guarantee Department. The Canadian Imperial Bank of Commerce also agreed to convert $100 million of its Massey loans to preferred shares, and to purchase an additional $50 million of the new preferreds for cash.

An agreement with the banks was a prerequisite to arranging federal and provincial support. Massey president Victor Rice now returned to the governments. In February 1981 the government portion of the bailout was finally arranged. The Ontario and federal governments would guarantee a sale of preferred shares worth $200 million. The Ontario

government would guarantee $75 million and the federal government would guarantee $125 million. The preferred shares were to be sold for $25 a share and paid a dividend of half prime plus 1-3/8 per cent. In addition, 25 million warrants were to be sold at 50 cents per warrant. The warrants were for the purchase of Massey common stock at $5 per share and were exercisable over ten years. If the warrant was used to buy a Massey common share within two years, the purchaser would receive an additional identical warrant. The common-stock exercise price (for this free warrant) was $4 for one year, at which time the $5 common-stock price became effective again. The government guarantee was to be implemented only if Massey failed to meet a monthly dividend payment on the guaranteed preferred shares. In the event of a default, holders could claim the issue price of $25 per share plus back dividends.

In return for the government assistance, Massey promised:

> to maintain or expand production in Canada; if economically feasible, to focus new investment in North America; to maintain the Canadian labour force at 13 per cent of the worldwide labour force; not to reduce the Canadian labour force below 6,000 except for temporary layoffs; to set up an engineering and research centre in Canada.[32]

Having arranged the bailout terms, the next step was to get Cabinet approval. At the federal level, the Trudeau government chose not to face Parliament with the issue of its support of a major multinational corporation. Instead, it decided to '. . . rely on existing powers to provide a guarantee in the event of Massey's failure to meet its commitments.' Although extensive parliamentary debate was therefore avoided, federal involvement was still not assured. The federal cabinet split on the Massey issue and Prime Minister Trudeau finally made the federal decision to bail out Massey.[33] The *Economist* suggested a number of possible motivations for federal assistance to Massey. First, although 5,000 of the Massey Ferguson jobs were in Ontario, another 6,000 dealers could be hurt by a Massey bankruptcy. Secondly, with 80 per cent of Canadian production being exported, a Massey failure would have had an impact on the balance of payments. Thirdly, a Massey bankruptcy would be the end of a locally based farm equipment manufacturer.[34]

At the provincial level, the bailout had to meet with legislative approval. There appears to have been general agreement among the

three provincial parties that Massey should be bailed out. Although the NDP objected to the lack of firm job guarantees, debate on the issue was weak. On 5 May 1981 Larry Grossman gave first reading of Bill 48, the Massey-Ferguson Limited Act.[35] The Act would authorize Ontario to purchase shares of Massey should this be required under the terms of the agreements to be entered into between Massey, Ottawa, and Toronto. The federal and provincial governments might be required to purchase from the shareholders up to 8 million series D preferred shares with a stated value of $25. Canada's and Ontario's liabilities were apportioned at 62.5 per cent and 37.5 per cent respectively with Ontario's dollar liability not to exceed $78 million. These guarantees were expected to enable Massey Ferguson to complete its refinancing package which totalled in excess of $700 million. The guarantees were to be implemented only if Massey failed to meet a monthly dividend payment on the guaranteed preferred shares.

The Ontario NDP was opposed to the Act on the principle that it could not approve legislation before an agreement between Massey and the Canadian and Ontario governments was tabled. David Cooke, MPP (NDP) reaffirmed the NDP's commitment to saving jobs and its understanding of the importance of the farm-machinery industry.[36] However, the legislature still knew nothing about an agreement and therefore could not authorize Ontario to guarantee $78 million in shares. MPP's questioned Massey Ferguson's long-term business viability. They had no information on whether the guarantee was a good deal. Massey's commitments on jobs and parts sourcing lacked specificity. However, the Act passed without amendment on 2 June 1981 carried by the Liberals and PC's. The debate on the Act had followed the NDP's loss of the Brantford riding in a May by-election in which M. Maliachuk lost to the Conservative P.A. Gillies.

The final requirement for the rescue operation's success was the sale of shares. Dominion Securities Ames (then A.E. Ames) had assured Massey that the issue would be taken up within ten days. However, some obstacles remained before the issue could be fully sold. Revenue Canada was called upon to re-enact income tax-free status for preferred shares. In the previous budget, this tax treatment (applicable to financial institutions) had been removed. After Massey's refinancing scheme was presented it was reapplied for financially troubled businesses. This taxation assistance meant that, during this period, Massey's share return was 19 per cent compared to 13.5 per cent for Canadian Savings

Bonds. Even with the appeal of the return and the government guarantee, the issue was still not sold until 24 April 1981. To appeal to the market, the company had to do two things. First, they increased the yield from half of prime plus .75 per cent to half of prime plus 1.375 per cent. Second, they reduced the price of the warrant from 50 cents to 25 cents.[37]

The federal government had been cool to Massey from the beginning of the company's financial problems. First, the federal government had not been receptive to Conrad Black's diesel-engine development scheme which could have made Massey a more viable company. Black felt that establishment of a diesel facility would make Massey less vulnerable to currency fluctuations and the effect these fluctuations have on Massey's parts-sourcing costs. Black proposed a $600 million investment in which Argus would invest $150 million. In a letter to Herb Gray, Black stated 'Massey Ferguson has a terrible track record as an investment and is now in desperate straits. However, we know Massey Ferguson well and would be willing to invest in it under conditions no less rigorous than those the government itself would impose.'[38] Black was aware of the reservations to government involvement in the diesel venture. Black stated first,

> that the federal government is unconvinced that the private sector has been exhausted . . . if the deal is good enough for us (Argus) why wouldn't the rest of the private sector be crowding forward, second, that any federal government support would inevitably give Argus Corporation a riskfree sleighride, third, that the federal government can't really afford to extend assistance now and such assistance would be a bad and dangerous precedent, fourth, that Massey Ferguson is not really a Canadian Company in terms of employment, production, research and exports, and fifth, that no amount of money would stabilize a company with such a spend-thrift history and that there is insufficient support for any aid to Massey.

In addition, Black also admitted that 'the present Argus owners are thought to be the "continuators" of their forebears who attacked Liberal governments of the past and all they stood for.'[39]

In his correspondence with Herb Gray, Black referred frequently to the positive provincial support of the Ontario government for the Massey-Chrysler diesel venture. But getting the Conservative support

was easier for Black since he had always been a big financial supporter of the Conservative government.[40] Although the diesel engine lost its attraction as oil prices fell, the diesel was still attractive during this period.

The unattractive investment features of the initial bailout proposal indicated a lack of commitment to Massey. Perhaps the federal government was skeptical of Massey's ability to pull through. The industry was threatened by many shaky companies and each potential bankruptcy undermined the viability of other farm-equipment manufacturers. For example, International Harvester is still performing poorly and is therefore a candidate for insolvency. It too has been refinanced by its banker. The possibility of Harvester's finished-goods inventory being dumped on the market has been a great concern; it would damage Massey's already depressed sales. Over the long term Massey might be able to improve its market share by a Harvester insolvency, but the immediate impact of low-priced inventory being dumped on the market would have an adverse effect on Massey's already slumping sales.

THE POST-BAILOUT PERIOD

The bailout was finally signed in July 1981, but Massey's performance since the bailout has not been encouraging. In 1981, total Massey worldwide sales fell 16 per cent. Without sufficient revenue to cover costs, Massey was again in a tight cash position. The 1981 working day record was not good either. In mid-November 1981, 1,450 people were laid off in Brantford and 300 in Toronto. When an additional 400 were laid off in December the majority of Massey's Canadian workforce was not working. In total 3,700 were on layoff with the earliest recall set for February 1982.

In March 1982 White Farm Equipment suspended its manufacturing operations, laying off 740 hourly and 185 salaried workers. White had already received $20 million in loan guarantees and concessions from its employees but was not able to maintain profitable operations. The company was sold to a Texas firm but the federal government vetoed the sale. Although there were 1,000 jobs at stake Herb Gray did not want the company to become another American subsidiary. However, the Ontario government pushed for the sale which finally came through and by early May its employment was up to pre-shutdown levels. That same

month International Harvester put 1,500 workers on a month's layoff and by June, White was again laying off.

With the industry in such disarray, Massey's financial problems increased. In order to save $48 million, Massey suspended payments of its monthly dividend on the new issue of preferred shares. Under the terms of the bailout the governments were forced to honour their guarantees and purchase the new issue of preferred shares of Massey. In the summer of 1982, the federal government had acquired a 7 per cent interest in Massey, the Ontario government a 3.65 per cent interest, and the British government a 4.2 per cent interest for $125 million, $75 million and $90 million respectively.

On 6 July 1982 Gordon Walker (who replaced Grossman as the provincial Minister of Industry and Tourism) announced that Ontario had purchased 3 million series D preferred shares. It did so once Massey failed to pay a monthly dividend in June 1982. Ontario paid $75,809,614 to the trustee for the holders (National Trust), and then had no further obligations under the Massey Ferguson Limited Act. He stated that McLeod, Young, Weir Ltd., informed Ontario that it was impossible to assess the present market value of series D shares since Massey's financial position was not clear.[41] Ontario had not yet decided to have anyone serve on Massey's board of directors, although the NDP was pressing the government to do so. At the time of the bailout Ontario was receiving information on Massey, and monitoring the firm under arrangements with the federal government which permitted Ontario full access to Ottawa's information.

Besides suspending dividends and hence forcing the governments to implement their guarantees, Massey may have been in breach of other conditions of the bailout. For example, it is not clear whether or not the employment conditions of the bailout had been complied with. In the fall of 1981 concern was expressed in the Legislature regarding Massey's announced indefinite layoffs of 600 in Brantford. Stuart Smith (Ontario Liberal leader) expressed the view that this was not permitted under the agreement which only allowed temporary layoffs. Grossman countered that this depended on the definition of temporary.[42] On 2 November 1981 Grossman refused to table the layoff agreement stating that this would hurt Massey's competitive position. Indeed, Massey was continuing to lose money and public awareness of this might have deepened the crisis of confidence in the company.[43] In August 1982 the *Toronto Star* reported that the production line at Massey had operated for only five of

the last ten months (and then on a reduced shift basis).[44] Salaried workers were also suffering. In December 1981 all of Massey's Canadian salaried workers had their wages frozen. In June 1982 some salaried personnel agreed to a 25 per cent deferral of their salaries and others agreed to a 20 per cent deferral (to be repaid within three months).

By the end of 1982, the Massey workforce worldwide had shrunk to 29,749 employees from 39,789 at the end of 1981. At a shareholders meeting in April 1983, Victor Rice told the shareholders that the Toronto facilities (employing 1,200 workers) would be closed. However, Rice pointed out that if this was done the Brantford facilities would be expanded. Although within the requirement of 13 per cent of total workers, the loss of 1,200 workers could put Massey in violation of the bailout agreement. As published in the 1981 financial statements, 'Massey agreed to maintain 6,000 employees in Canada'.

Since the bailout, Massey has tried desperately to reduce expenses in order to conserve cash. Massey's leaner operations and control of costs are apparent if one looks at Massey manufacturing operations rather than their bottom line. In 1980 funds 'used' in operations were $420.2 million. In 1981 funds 'provided' by operations were $27.3 million and, in 1982, funds 'provided' by operations were $21.4 million. The Statement of Changes in Financial Position from the 1982 financial statement (see Table 9) shows the Massey cash position. Massey's current bottom-line performance is not wholly a reflection of management's inability to rationalize operations. Rather Massey's current problems are the result of past bad management and the current depressed market for farm equipment.

By 1982 Massey was in trouble again (see Table 7). The Z score shows that Massey again had a bankruptcy classification. Massey negotiated a second restructuring. This restructuring saved Massey $620 million:

1 $230 million comes from interest which is being waived by certain lenders in return for common shares.
2 $166 million comes from debt converted to common shares.
3 The government of France, together with several French banks, lent $49 million in return for guarantees of continued tractor exports from France.
4 Holders of preferred shares bought under the 1981 refinancing plan received common shares in lieu of $75 million in cash dividends.

TABLE 9

Consolidated statements of changes in financial position
Massey Ferguson Limited (millions of US dollars)

	Three months ended 31 January		Year ended 31 January	Years ended 31 October		
	1983	1982 (unaudited)	1984	1982	1981	1980
Cash provided by (used in) operations (note 17(c))	$(5.7)	$(47.0)	$44.8	$21.4	$27.3	$(420.2)
Other sources of cash						
Investment transactions:						
Disposal of investments in associate companies	–	–	–	–	24.2	41.7
Disposal of fixed assets	4.9	0.6	2.6	11.5	10.1	34.1
Financing transactions:						
Refinancing:						
Issue of preferred shares (and warrants in 1981)	–	39.9	–	78.8	290.2	–
Interest and principal waiver and conversion program						
– contributed surplus	–	–	–	–	51.5	–
– common shares issued	1.3	7.5	22.5	18.5	31.9	–
– other paid-in capital	–	–	21.2	–	–	–
Costs of restructure	(0.1)	(0.1)	(7.8)	(0.4)	(12.6)	–
Total refinancing	1.2	47.3	35.9	96.9	361.0	–
Increases in long-term debt	32.3	18.4	43.6	52.2	10.6	–
Increase in bank borrowings and current portion of long-term debt	–	17.9	32.3	–	–	504.3
Increase in due to unconsolidated subsidiaries	–	–	20.8	–	–	–
Total other sources of cash	38.4	84.2	135.2	160.6	405.9	580.1

TABLE 9 (continued)

	Three months ended 31 January		Year ended 31 January	Years ended 31 October		
	1983	1982 (unaudited)	1984	1982	1981	1980
Other uses of cash						
Investment transactions:						
Additions to fixed assets	5.3	7.5	36.3	47.4	43.6	46.2
Investment in unconsolidated subsidiaries and associate companies	0.3	0.3	3.0	0.7	7.2	0.4
Increase in other assets and deferred charges	6.7	0.1	18.7	13.4	5.7	4.8
Other	2.2	1.9	2.6	3.6	2.8	2.4
Financing transactions:						
Reductions in long-term debt	5.8	17.9	155.4	39.4	92.0	67.1
Reduction in bank borrowings and current portion of long-term debt	23.6	–	–	12.2	261.4	–
Cash dividends paid	–	9.6	–	22.4	11.5	–
Total other uses of cash	43.9	37.3	216.0	139.1	424.2	120.9
(Decrease) increase in cash and short-term investments during the period	(11.2)	(0.1)	(36.0)	42.9	9.0	39.0
Cash and short-term investments at beginning of period	108.1	65.2	96.9	65.2	56.2	17.2
Cash and short-term investments at end of period	$96.9	$65.1	$60.9	$108.1	$65.2	$56.2

SOURCE: Massey Ferguson Limited annual reports 1983 and 1982.

In an effort to save $9 million in interest on preferred shares of class A and class B stock, Massey Ferguson offered to convert its preferred A and B shares into common stock. This effort met resistance in May 1983 as 51 per cent of the class A and class B shareholders rejected the company's offer.[45] During the second restructuring effort, there was no indication that the Ontario or federal governments were approached. They did, however, agree to waive dividends.

Massey's intention now is to register the warrants and the related common shares for trading in the United States subject to the filing of certain documents with the US Securities and Exchange Commission. Massey shares had been ledgered. This means that the shares are not transferable in the United States or to US citizens, nationals, or residents. This restriction has recently been lifted. The two-year period for the free-warrant privilege would have expired on 31 May 1983 but it was extended to February 1984. The warrants are another attempt by Massey to acquire some quick cash. With 25 million outstanding warrants, $12.5 million could be generated plus $100 million if the free warrants are exercised at the $4 price. The restriction was lifted prior to the February 1984 date.

The company also tried to improve its financial position when its collective agreement expired on 1 September 1983. Massey wanted significant concessions from its workforce, including the elimination of the COLA clause and reduction of vacation pay. Despite the depressed industry, Canadian workers refused these demands saying that the cost saving would be insignificant relative to Massey's problems. A two-day strike ensued and a settlement was reached on 11 September which essentially extended the old agreement and provided for new major concessions.[46]

Since Massey's troubles began in 1978, Massey has lost $1.1 billion. Massey's president, Victor Rice, is again forecasting a sales upswing next year. He feels farmers have deferred major purchases and will soon be buying again. However, North American farm income fell 44 per cent between 1979 and 1982.[47] In 1980 Massey made forecasts for three years.[48] The first forecast was that the deficit for 1980 would be $90 million. The deficit *reported* in 1980 was $225 million. The second prediction was an $8 million profit for 1981. The deficit for 1981 was $194.8 million. The forecast for 1982 was a $200 million profit. Massey lost $413.2 million in 1982. For the year ended 31 January 1984 Massey had

reduced its loss to $68 million. First quarter 1984 showed a $2.4 million profit and the second quarter of 1984 showed a $7.4 million profit.[49]

Massey is still in a precarious position. From 1977 to the fiscal year ended 31 January 1984, Massey had accumulated losses of $1.2 billion US according to the *Financial Post* Investment databank. By 1978, unit sales had dropped 30 per cent from the high in 1976, combines had plunged 50 per cent and industrial sales were down almost 70 per cent from the 1978 high.[50] The success of the original bailout remains unclear. Massey's value to its original shareholders is virtually nil. With full dilution of shares there would be 216.6 million shares outstanding. Massey's only value may be to potential owners who would be buying more efficient operations and years of tax write-offs. Massey is also attractive as an innovator. It is heavily involved with the development of electronics in agriculture. Massey has apparently maintained its research and development facilities even though it has downsized a lot of other facilities.[51] In the fall of 1983, Massey also purchased the Rolls Royce diesel-manufacturing plant in England. China is also part of Massey strategy. The company plans US distribution of a small diesel engine manufactured in China.[52]

The industry in general is much smaller. 'Massey has held its market share but the pie is much smaller than in 1976.'[53] When the industry recovers, however, Victor Rice claims that Massey will be ready in spite of its rationalization.

NOTES

1 Cook, Peter (1981) *Massey at the Brink* (Collins: Toronto) 74, 104.
2 Ibid., 179, 204.
3 Baldwin, Carliss, and Scott Mason (1980) 'Massey Ferguson', Harvard Business School Case Study 1982, 4; Barber, Clarence (1971) *Royal Commission on Farm Machinery* (Ottawa: Information Canada).
4 *Executive*, August 1980, 26.
5 'Cliff hanger at Massey Ferguson', *Business Week*, 20 October 1980, 112.
6 Newman, Peter (1982) *The Establishment Man: A Portrait of Power* (Toronto: McClelland and Stewart) 302.
7 *Economist*, 24 October 1980.
8 *Financial Post*, 2 October, 1982.

9 *Toronto Star*, 13 August 1980.
10 *Canadian Business*, June 1981, 138.
11 *Financial Post*, 6 September 1980.
12 Ibid., 15 December 1980.
13 Horvitch, Sonita (1980) 'Bankers walk Massey tightrope' *Financial Post* 13 September.
14 Evans, Eric (1980) 'Massey: the negotiations continue'. *Financial Post* 13 September.
15 *Financial Times*, 22 December 1980.
16 See White Farm Equipment case study.
17 *Toronto Star*, 13 August 1980.
18 *Hamilton Spectator*, 31 May 1980.
19 Ibid., February 1982.
20 *Toronto Star*, 3 December 1980.
21 Legislature of Ontario Debates 16 October 1980.
22 Ibid., 6 October 1980.
23 Ibid., 16–17 October 1980.
24 Ibid., 30 May 1980.
25 Ibid., 10 December 1980
26 Ibid., 7 October 1980.
27 Ibid., 3 June 1980.
28 Ibid., 30 May 1980.
29 Ibid., 22 October 1980.
30 Ibid., 9 February 1981.
31 *Wall Street Journal*, 21 October 1980.
32 *Globe and Mail*, 11 February 1981.
33 Cook (1981) op. cit., 15, 266.
34 *Economist* 11 october 1980, 82.
35 Legislature of Ontario Debates 5 May 1981.
36 Ibid., 26 May 1981.
37 *Globe and Mail*, 8 April 1981.
38 Newman (1982) op. cit.
39 Ibid., 312-313.
40 *Economist*, 25 October 1980.
41 Legislature of Ontario Debates 6 July 1982.
42 Ibid., 14 October, 29 October 1981.
43 Ibid., 2 November 1981.
44 *Toronto Star*, 17 August 1982.

45 The offer price was a number of common shares arrived at by dividing \$14.25 by the trading price of common over a five-day specified period. Since the original offer (which was not accepted because of lack of a quorum), the common-stock prices have increased from \$4.50 to \$7.75. When the plan was rejected, the preferred shareholders would therefore have received fewer common shares because of the price increase.
46 *Globe and Mail* 12 September 1983.
47 Daw, J. (1982) 'Massey's loss second biggest ever'. *Toronto Star* 23 December.
48 *Industrial Marketing* July 1982, 18.
49 Spears, John (1984) 'Massey harvests its second profit'. *Toronto Star* 5 September.
50 Wilmott, Tessa (1984) 'Companies on the comeback'. *Financial Post* 29 December.
51 Hunter, Nicholas (1983) 'Massey turning to electronics to keep a step ahead'. *Globe and Mail* 8 July.
52 *Financial Times* 'The gruelling process continues'. 23 January 1984.
53 Evans, Eric (1983) 'Massey-Ferguson emerging from fire trough' *Financial Post* 1 January.

3
Canadair Ltd.

INTRODUCTION

In 1947 the Electric Boat Company of Connecticut, a submarine manufacturer, purchased almost all of the stock in Canadair Ltd. from the Canadian government. The Crown had acquired the aircraft division of British-owned Canadian Vickers Ltd. in 1942. This entity became Canadair Ltd. in 1944. The apparent purpose of this purchase by the government had been to ensure a supply of military aircraft and components during the war. When this function was no longer necessary, Canadair was returned to the private sector.

The Electric Boat Company was the predecessor of General Dynamics Corporation from whom the government repurchased Canadair in January 1976. Canadair was operated as a commercial enterprise under the Canada Business Corporations Act; the government was sole shareholder and appointed the board. In November 1982, the Crown's shares were transferred to the Canada Development Investment Corporation (CDIC)[1] whose mandate is to operate the company within a commercial framework.[2] It is assigned the task of finding solutions to the difficulties of Canadair which were identified by the government in 1981 and 1982 task-force reports. These reports are classified as cabinet documents and have not been released to the public. Recently, the new federal government announced that CDIC will attempt to find a private buyer for Canadair.

BACKGROUND

Canadair is based in Ville St. Laurent, Quebec and is a developer and manufacturer of battlefield surveillance systems, the CL-215 water bomber, and the Challenger executive jet. It is one of nine companies which accounted for 60 per cent of total Canadian aerospace sales in 1976[3] Eighty to ninety per cent of Canadair's output is exported.[4] The bulk of exported products is sent to the United States.

Canadair acts as a subcontractor for a number of companies including Boeing and Lockheed as a supplier of airframe parts. As classified in the *Report of the Aerospace Manufacturing Sector Consultative Task Force* of 30 June 1978, Canadair is a first-tier company in the aerospace industry. It possesses an integrated capability to design, develop, manufacture and market complete aircraft. Canadair purchases some of its components from companies located throughout Canada. However, 40 to 70 per cent of the dollar value of components purchased by the industry is imported because there are basically no aircraft raw materials available in Canada. (For financial statistics see Appendices I to IV.)

The history of DeHavilland Aircraft of Canada Ltd. as a first-tier company is rather similar to that of Canadair and bears brief mention. DeHavilland was purchased by the federal government in 1974 when Ottawa exercised its option to acquire the company following federal participation in the development of the Dash-7; a fifty-seat commuter aircraft with STOL (short take-off and landing) capability. DeHavilland's British parent, Hawker Siddeley, had refused to participate, in part because it perceived the Dash-7 as competition for its own BAE-748 and in part because of doubts about the ability of the Dash-7 as a STOL rather than a general commuter aircraft. The Dash-7 failed to reach its sale expectations when the commuter market nosedived in the 1980s and in early 1983 the company concluded that it could not break even. Only eighty-eight aircraft had been sold and the company faced a deficit of $470 million. In September 1980 the Dash-8, a thirty-six seat aircraft, entered development with an estimated cost of $270 million and a break-even estimate of 185 sales. Development was financed by $450 million in federal loan guarantees and $260 million in equity. In the seven months ended 31 December 1982 the Dash-8 had caused DeHavilland to report losses of $266.1 million, with a $196.5 million writeoff of capitalized costs from previous years. On 26 November 1982 the government's shares in DeHavilland were transferred to the Canada Development Investment

Corporation. The CDIC has expressed a commitment to continue with the development of the Dash-8. Requests have been made to Parliament for the approval of direct equity support to avoid the interest burden of loan guarantees. Senator Jack Austin, the minister formerly responsible for CDIC has asserted that the Dash-8 is viable. However, it has many competitors which receive public funding, and subsidies are required to place DeHavilland on an equal footing.

Canadair has received public assistance in some form for the past two decades. As a private-sector company from 1947-76, the company relied on federal defence orders[5] and subsidies through a number of federal programs. Federal grants to Canadair totalled $31,454,026 from 1965/66 to 1969/70 and $22,255,207.89 from 1970/71 to 1974/75.[6] The total value of government grants to Canadair was $68,447,953 by October 1975.[7]

The Department of National Defense also purchased jet trainers and fighter aircraft during the period 1947-75. In November 1975 Canadair received subcontract work on the Lockheed Long Range Patrol Aircraft to be built for the Canadian Armed Forces.[8]

The company's dependence on military sales was the source of a great many of its financial difficulties in the 1970s. Military orders from the Canadian forces had declined in the late 1960s as procurement budgets fell. General Dynamics Corportion had channelled its decreasing numbers of contracts to its US plants, and not to Canadair. Officials of Canadair therefore concluded that 'foreign ownership was restricting [its] freedom of decision-making and action.'[9] Canadair's difficulties reflected the general decline of the aircraft industry in Canada. Employment fell from a company peak of 13,495 in 1953 to 2,400 in 1974. Sales in 1974 were down to $43 million from $138 million in 1959.[10]

In 1974 Frederick Kearns, president of Canadair Ltd., approached Ottawa to purchase Canadair from General Dynamics Corporation. He had sought a private takeover, but had received no realistc offers.[11] Without a formal government response Canadair would continue its decline.

The actors

Key private-sector actors involved in the decisions on Canadair from 1975-73 have been Frederick Kearns (past-president of Canadair) and Gil Bennett (interim president, Canadair, and vice-president, Canada Development Investment Corporation). Spokesmen for the industry

have included David Mundy and Jacques Desroches (past-presidents of the Air Industries Association of Canada), and Max Ward (president of Wardair Canada). Union members and leaders have not taken prominent public positions on the problems of Canadair.

In the public sector the departments of National Defence and Industry, Trade and Commerce have been heavily involved in Canadair's fortunes. Cabinet members have included the past ministers of Industry, Trade and Commerce Don Jamieson, Jean Chrétien, Robert de Cotret, Herb Gray, and Ed Lumley. Senator Jack Austin, Minister of State for Social Development and the minister responsible to Parliament for CDIC, defended continued government aid to Canadair. Prime Minister Trudeau also actively supported further assistance to the company, while Auditor-General Kenneth Dye attempted to instil a note of caution in public and in such parliamentary forums as the hearings of the Public Accounts Committee.

Maurice Strong and Joel Bell were chairman and president of the Canada Development Investment Corporation respectively.

Joe Clark expressed support for the privatization of Canadair during his tenure as prime minister, and he was joined by Sinclair Stevens, then president of the Treasury Board, who has been a strong critic of Canadair since 1976. Don Blenkarn MP, Pat Carney MP, Ian Deans MP, Walter Baker MP, and NDP leader Ed Broadbent have been active in recent criticisms of Canadair. They have been joined by a Liberal backbencher, James Peterson, a member of the House of Commons Finance Committee. The Quebec government was involved until a possible $20 million provincial loan guarantee to Canadair for the Challenger project was rejected by the board of Canadair in July 1977.

CANADAIR AS A CROWN CORPORATION

The decision to revert from a policy of subsidies to public ownership constitutes a bailout of a failing private-sector corporation. Ottawa's adoption of public ownership in response to Kearns's request for aid to Canadair followed a debate which centred on the fate of the entire Canadian aircraft industry. In 1974 the Crown had purchased DeHavilland Aircraft of Canada Ltd. as a step towards the industry's rationalization and re-organization. Ottawa was attempting to develop a coherent strategy toward a high-technology sector which was competitive in the world market and which provided significant employment.

In 1973 the federal government had received three proposals from the private sector regarding the purchase of the two companies. Air Canada had proposed a partnership with Canadian International Comstock Co. to take over the companies.

Spar Aerospace Products Ltd. and S.B. McLaughlin Associates Ltd. had also expressed interest.[12] Alastair Gillespie, the Minister of Energy, advocated a private-sector purchase of both companies.[13] However, he stated that since the industry needs public funds for development all profits should stay in Canada.

On 15 January 1975 the federal government through the Department of Industry, Trade and Commerce, signed an option agreement indicating the government's intent to consider the repurchase of Canadair from General Dynamics.[14] The option was due to expire in early December 1975.

The issue was not strongly debated in the press or in the House of Commons. Opposition members appeared most concerned with the future corporate structure of the industry.[15] Canadair as a firm was considered only within the context of the survival and growth of the Canadian aerospace industry since Canadair at the time was one of only two aircraft manufacturers in Canada.[16]

On 19 December 1975 Don Jamieson (then Minister of Industry, Trade and Commerce) announced in the House of Commons that the federal government would exercise its option to purchase Canadair. This was reconciled with the government's repeated assurances that it had no desire to remain permanently in the aircraft industry by the commitment that both DeHavilland and Canadair would revert to the private sector once their survival was assured.[17] Marcel Roy (Parliamentary Secretary to the Minister of ITC) quoted Jamieson that '. . . this way there will be excellent possibilities of restructuring the aircraft industry in Canada, getting a stable industry more controlled by Canadians, [and] developing excellent capabilities in the area of specialized commercial aircraft.'[18] This rationale was re-affirmed by Senator Austin in his June 1983 report wherein he stated that the government acted to preserve Canada's ability to produce aircraft, encourage the export role of the aerospace sector, save jobs and maintain the market for high- technology component manufacturing.[19]

On 5 January 1976 Canadair was purchased for $38,150,000.[20] The board of directors would be replaced with an interim board, and then a decision would be made on an approach to the private sector. In

November 1976 David Golden who had served as a president of the Air Industries Association of Canada and was then president of Telesat Canada, was appointed to examine whether Canadair and DeHavilland would be profitable.[21] His study was due for completion in late 1978, but has not been publicly released. To date, DeHavilland and Canadair have not been restructured under any reorganization of the aerospace industry.

The impact of public ownership

Canadair has continued to receive extensive public assistance as a Crown corporation. Its relationship with the government has undergone two major re-alignments; the first being public ownership, the second the transfer of Canadair to the CDIC. The period of public ownership will now be examined.

Canadair's development of the Challenger executive jet

Following the government's acquisition of Canadair, Fred Kearns, then president of Canadair Ltd., decided that a new product line was needed to escape the 'boom and bust' nature of military production.[22] He noted that business jet sales were continuing despite the decline in the aerospace market, and that the business jet market was perceived as an industry growth centre.[23] 'The [Challenger] was crying out to be built . . . there had been nothing new in the business jet field for fifteen years so we decided to put the new technology together.'[24] Canadair acquired exclusive rights to the jet design from William Lear for the Learstar 600, which was to become the Challenger 600. However, Canadair had never undertaken a project of this magnitude or complexity and it realized that entry into the market would be costly. Canadair's engineering staff was also at a record low of 150. Lear added to the uncertainty by leaving the project following design changes by Canadair which widened the jet, increasing its market attractiveness but making it heavier and less fuel efficient. Canadair also encountered problems by attempting to rush the design-to-production process. The company wanted the Challenger produced in thirty months instead of the normal industry period of five years. Its difficulties were compounded when Avco-Lycoming, the company supplying the engine for the Challenger, could not meet delivery dates. In addition, the engine did not function efficiently. Essentially, 'the plane cost more and took longer to develop than was expected, failed

to meet its presold specifications, was delayed because of problems with its initial engine manufacturer and in the certification process, encountered break-in-problems, failed to achieve projected sales targets and ran head-on into the recent global recession.[25]

On 1 November 1976 Jean Chrétien, then Minister of Industry, Trade and Commerce, announced that the federal government would back the Challenger program. Canadair required $125 million in order to begin the project and Ottawa announced its willingness to guarantee half the amount.[26] The Canadian Imperial Bank of Commerce and the Provincial Bank of Canada provided $62.5 million on Canadair's credit alone.[27] On 15 October 1976 Ottawa had made an agreement with the Quebec Liberal government that Ottawa would provide a $50 million loan guarantee, while Quebec guaranteed $20 million. On 15 November 1976 the Parti Québécois was elected and subsequently toughened the conditions of the guarantee.[28] It demanded two government members on the board of directors whose purpose was to ensure that subcontracts were awarded in the interests of Quebec. Membership on the executive committee was also stipulated. Canadair refused the new conditions and arranged financing without Quebec through additional participation by Ottawa.

To acquire the program go-ahead and the guarantee, Canadair had to demonstrate that there were over fifty orders for the Challenger jet. At this early stage, sales had taken on a life-or-death importance for the project. Guarantees were written into sales contracts specifying speed, take-off and landing distance far superior to the competition.[29] A deposit of 5 per cent of the purchase price would be returned if these specifications were not met. In its determination to make sales, Canadair entered into a number of deals which have been criticized in hindsight.

When it was first produced in 1977, the Challenger 600 was priced at $4.25 million US. Its present selling price is over $11 million Canadian. Pierre Deniger, MP and a member of the Standing Committee on Public Accounts, alleged that 'a person on welfare could have put in an order for one of [their] planes and not suffered any loss'.[30] Deposits were often returned, occasionally at interest rates higher than the banks were paying, becaue the design failed to meet specifications.

Canadair had hired a proven marketing expert, Jim Taylor (who led the highly successful Falcon and Cessna Citation marketing efforts). The Challenger's marketing headquarters were established as a subsidiary in the United States to serve its largest potential market.

Marketing efforts were extensive and costly.[31] Thus, the low selling price and the aggressive marketing program were designed to encourage early buyers. Unfortunately, many sales were not consummated.

Canadair claimed that 109 Challengers were ordered before November 1978.[32] Since it had forecast its bread-even level at 136 aircraft the company appeared well on its way to success. Canadair had also forecast that the Challenger could be brought to commercial production for $106 million with peak financial requirements of $128 million by the fall of 1979. The government's basis for assistance had been the company's claim that by mid-1982 all development costs would be recovered.[33]

Perhaps the most widely criticized deal was that which Canadair made with Federal Express Ltd. of Memphis, Tennessee, a courier company. The circumstances surrounding this deal were revealed in detail in Federal Express's annual report and in the CBC's *Fifth Estate* program on 13 April 1983. Federal Express ordered twenty-five Challengers from Canadair in 1976 and paid a token deposit of $250,000, the normal deposit for one plane.[34] In 1977 the rules for couriers were changed and Federal Express was permitted to fly larger aircraft, and therefore had no need for the Challenger. By January 1978 Federal Express had made a loose agreement to purchase the Challenger 610, a stretched version of the 600. However, this aircraft program was cancelled in March 1980.[35] Federal Express then dropped its order to five planes, and eventually one, by March 1978. Under a new agreement Canadair was to resell the remaining twenty-four aircraft and turn the profit over to Federal Express, using the rationale that Canadair did not want lower-priced planes on the market. By late 1982 Federal Express had, in effect, received one free plane and $4.375 million from Canadair.[36] Fred Kearns stated, 'we thought we had driven a very hard bargain'[37] (in terms of keeping Federal Express from selling planes in competition with Canadair). In the House of Commons on 13 April 1983 Ed Broadbent, NDP leader, demanded a full public inquiry into allegations that Canadair faked orders and misled the House Finance Committee in terms of claims for sales.[38] In what has become a standard reply, Pierre Bussières, Minister of National Revenue, stated that the CDIC will improve management.

Canadair was also involved in problematic deals with its Middle East distributor TAG (Technique Avant Garde). TAG refused to take twenty-five planes it had ordered because they failed to meet specifications. However, one aircraft in an unfinished condition (i.e., interior outfitting,

unpainted, and lacking certain avionics) was bought by TAG at an earlier date for $5.6 million US and then resold to Canadair for $10 million (including interior outfitting and avionics). Canadair's involvement in a bribery scandal involving allegations that one of the company's representatives had bribed Senator George Hohman of Alaska in an attempt to have Alaska purchase two CL-215 water bombers did not improve the company's credibility.[39]

The apparently healthy state of Canadair's order books (see Appendix V) created an atmosphere of buoyancy and optimism until 1981-2. The Challenger had been repeatedly modified, with a number of changes made after the plane was in the hands of its first customers. Design changes eventually cost the company $300 million,[40] and delayed the delivery schedule, which resulted in cancelled orders. Parts in production were scrapped and suppliers were paid for parts that could not be used.[41]

The Challenger was not certified by the Canadian Ministry of Transport until August 1980. In the same period Canadair experienced problems with the Avco-Lycoming engine, as the Lycoming company continually failed to meet delivery dates, thus slowing the Challenger's production schedule.[42] In March 1980 Canadair launched the Challenger 601 to add to the 600, with a General Electric engine to replace the Lycoming engine. The more powerful GE engine would boost the range of the jet. When the stretched Challenger 610 program was cancelled, GE raised the price of Canadair's order by 19 per cent and demanded the order be doubled from 100 to 200 because the original contract had included engines for the 610; now the order was to serve only the Challenger 601. It was alleged that Kearns did not inform the government of this increased cost and continued to insist that the company had no problems with the performance of Avco-Lycoming.[43] However, on 30 May 1983 Canadair announced that it was suing Avco-Lycoming for $109.6 million.[44] Avco-Lyoming in turn filed suit against Canadair for $100 million on 5 August 1983 for Canadair's alleged unilateral termination of a 1977 agreement to purchase engines for the Challenger 600.[45]

The Challenger and the workforce

The Challenger project has had a positive impact on employment at Canadair which peaked at 6,170 workers in June 1981.[46] When the

Challenger program was announced in November 1976 Jean Chrétien forecast that it would provide 1,500 direct and 1,500 indirect jobs.[47] By early 1983 over half of Canadair's employees were associated with the Challenger jet. Canadair has enjoyed peaceful relations with the union represented at the plant – the International Union of Machinists and Aerospace Workers. While DeHavilland has been plagued by strikes (there were three from July 1978 to July 1981), Canadair had signed long-term contracts in order to avoid production shutdowns, particularly in the rush to move the Challenger off the assembly line to meet delivery dates.[48]

In early 1982 the company opened a temporary recruiting office in London, England after a Canada-wide campaign had failed to turn up a sufficient number of experienced aeronautical engineers. Canadair stated that employees were imported because they possessed skills which were in short supply or were not available in Canada such as aerodynamicists, stress analysts, and structures-design engineers.[49]

Most layoffs in recent periods have been a direct result of the problems with the Challenger.[50] In an effort to combat the company's difficulties, in October 1982 Canadair imposed a 5 per cent pay deferral on its 2,500 salaried employees.[51] Company officials announced that the recession had put 'extreme pressure' on the company's financial situation. Fred Kearns, the president of Canadair Ltd., hoped that this move would save Canadair $4.6 million over the fifteen-month wage-deferral period, and added that a number of top management figures would have their salaries deferred by 10 per cent. By late October 1982, 1,700 workers had been laid off due to slowdowns in demand, leaving total employment under 6,000.[52]

THE DECISION-MAKING PROCESS – BAILOUT OF A CROWN CORPORATION

Canadair's financial circumstances

In the summer of 1983 the Canadian government provided Canadair with a further equity injection of $240 million. In light of the company's past performance, strong opposition was expressed by government and opposition politicians. Canadair's cash requirements had previously been met almost entirely by borrowing at a time when interest rates were high (see Appendix VI). Normally in the aviation business, funds for the development of new aircraft are raised through equity rather than debt. However, debt versus equity was not a major issue when the

Challenger program was initiated and only became an issue as delays occurred and cash-flow needs kept rising. The CL-215 water bomber and a C-5A subcontract from Lockheed were financed by borrowing; Canadair felt reasonably comfortable continuing this practice with the Challenger.[53] However, as costs rose, the Challenger's break-even level for sales rose (see Appendix V). The Clark government attempted to sell the company in 1980 but discovered that it was worth only $50 million.[54] This would have involved a loss for the government of $400 million, according to an evaluation by the Comptroller-General.

Over the six years from 1976-82, more than $1 billion was advanced to Canadair supported by letters of comfort signed by successive ministers of ITC, including Robert de Cotret of the Clark government.[55] Letters of comfort do not require parliamentary approval and were only approved after the fact on 31 March 1982. They were extended despite an unreleased 1975 study by ITC which concluded that Canadair had weak financial controls and no longer possessed the ability to design and build a new plane.[56] Ottawa viewed Canadair as a commercial corporation and applied very few or detailed oversight requirements to it. Canadair received the loan guarantees (letters of comfort) without clearly specified targets to be realized with the funds.[57]

In March 1982 Parliament was asked to raise Canadair's debt ceiling to $1.35 billion – the then current estimate of Canadair's peak financial requirements.[58] Senator Austin stated in his report to the Standing Committee on Public Accounts of the House of Commons:

> the debt ceiling will be exhausted in the next few weeks. Canadair cannot generate sufficient net cash flow from operations to meet its existing debt service costs. The company is currently paying monthly interest charges of $12.5 million. The money being sought ($240 million) will be contributed as equity since Canadair is incapable of servicing new debt.[59]

Although the legislation passed, it was met with opposition, particularly from Conservative MP Don Blenkarn who objected to the high level of the company's debt and its net income of only $3 million. Sinclair Stevens demanded a full public review of Canadair's request. He noted that a 1979 report on Crown corporations by the Comptroller-General stated that the government involvement in Canadair to 30 June 1979 including equity, loans and loan guarantees stood at $471.2 million.[60] This was

$408.3 million greater than the estimated liquidation value of the company's assets. Canadair's interest costs had totalled $143 million in 1981, and if the company had not carried $1.1 billion in development and inventory costs plus interest on its books as an asset, it would have lost $140 million.[61] This was the first hint of the problems to be encountered with Canadair's accounting methods. It is significant that Donald Johnston, President of the Treasury Board, stated that letters of comfort had become excessively prevalent and it was wrong for the government to make extended use of them since they are not reflected in the public records.[62]

In the House of Commons on 15 April 1983, Ian Waddell MP asked whether it was true that a 1981 cabinet task force reported that Canadair's 1981 liabilities were $986 million and would rise to $1.2 billion.[63] The report urged the government to seek proper authority from Parliament for the $1.2 billion advanced to Canadair in letters of comfort. Jean-Jacques Blais, then Minister of Supply and Services, replied that this was confidential cabinet information. Pierre Bussières, then Minister of National Revenue, stated that it could be revealed only in committee. In the minutes of the Public Accounts Committee Meetings of June 1983, a number of Canadair and government officials refused to reveal in public specifically requested marketing information on the company, stating that this would hurt the company's competitive position. The information was later disclosed privately to the committee.

Sinclair Stevens continued to suggest that the government knew Canadair was in trouble long before action was taken. Quoting the *Fifth Estate* program 13 April 1983 he alleged that Prime Minister Trudeau and the cabinet were informed in October 1982 that government involvement in Canadair would extend from $1.8 billion to $2.3 billion before development costs were met.[64] In this event, the program noted that it would have been cheaper to give every member of the Challenger workforce $600,000 per year for life. The government's $1.5 billion involvement in Canadair by mid-1982 was more than Ottawa had spent on all its job-creation and retraining programs in that year.[65] Jean Chrétien continued to defend the decision to help Canadair develop the Challenger as a high-technology product vital to Canada's future.

On 26 October 1982 the government approached Parliament for the approval of a $200 million equity injection into Canadair (and $200 million for DeHavilland). This was the first equity infusion provided to the company and was to be used to retire debt and bring the debt-equity

ratio into better balance. Sinclair Stevens protested that the House was being used as a rubber stamp and questioned whether Canadair was viable in view of its $1.5 billion debt exposure. Ed Lumley stated that Canadair would be viable, the government wished to move away from letters of comfort to help the company and that further questions would be answered when the estimates were brought forward. Don Blenkarn stated that he would fight the $200 million in aid since there were no approved provisions in the federal spending estimates or in any estimate files to authorize it.[66]

In April 1983 Trudeau admitted that the government had known by the fall of 1981 that Canadair was in difficulty.[67] The question became whether Canada could afford to allow an important sector to go 'belly up'. He believed that Canadians should not 'lose their nerve' in helping a high-technology industry.

Allegations that Canadair had been allowed to mislead the House, and that, indeed, the government had been misleading the House, were frequently made. In May 1983 Sinclair Stevens asked why Kearns was permitted to appear before the House Finance Committee in November 1982 and not disclose full information on Canadair, in particular, its sales estimates. Don Blenkarn noted that P.J. Aird, senior vice-president of Canadair, had certified to the Finance Committee on 16 November 1982 that Canadair had an after-tax profit of $1.435 million. Thorne-Riddell, Canadair's accountants, certified in 1981 that the company made an after-tax profit of over $3 million.[68] This statement had been used as a basis to raise the debt ceiling to $1.35 billion in March 1982. Trudeau's reply was that the company was over-optimistic. However, he said the matter would work itself out since the CDIC was now responsible. Blenkarn pursued the matter, wondering how Parliament could be asked to approve more funds when Canadair had not filed a capital budget with the government.[69]

Following the company's announcement on 7 June 1983 that it had lost $1,414,900,000[70] (the largest corporate loss in the history of a Canadian company), Liberal backbenchers added their protests concerning Canadair's affair. James Peterson MP, a member of the Finance Committee, expressed 'disgust' and said 'we feel we've had a job done on us'.[71] The impetus for this statement was that MPs had expected an additional two weeks before a vote on the $240 million for Canadair. However, Yvon Pinard, government House Leader, had declared June 14 the last supply day before the summer recess. Therefore the estimates were

automatically called and passed before the Finance Committee finished its hearings on why and how Canadair had lost $1.4 billion. Liberal MPs demanded the firing of top Canadair executives after the losses were announced.[72]

Explanations of Canadair's financial troubles[73]

Part of the financial controversy surrounding Canadair Ltd. revolves around the company's use of capitalization of development costs, particularly with the development of the Challenger aircraft. This capitalization method is known as program accounting. Senator Jack Austin, in his report to the Standing Committee on Public Accounts, stated that the practice was in wide use in the aviation industry. However, he said Canadair used the practice more 'aggressively' by capitalizing 'money borrowed to finance the Challenger program, marketing costs, commissions, royalties, and product support costs instead of deducting these from current revenues as other aviation companies have done'.[74]

In addition, many companies would then allocate these deferred costs against revenue using an average cost base. In other words, as sales began to materialize the total number of these sales would then have to be determined. The normal practice would be to take this capitalized (or deferred) cost and divide it by the total number of aircraft the company expected to sell. Thus, the average costs of each aircraft could be determined and matched against the number of aircraft sold. Canadair, however, projected program costs on an estimated break-even number of sales.

> In effect, the amount used to calculate Canadair's costs of sales each year has been the actual Challenger sales revenue for the year with the remaining excess of actual production costs and other expenses related to the Challenger program during the year over sales revenues being capitalized and carried as inventory.[75]

Senator Austin went on to say that 'the accounting result has been that Canadair has reported a breakeven position on the Challenger program for 1981 and prior years when other aviation companies in similar circumstances would have reported losses.

As explained in the notes to the company's 1982 financial statements, program accounting is used to even out the earnings stream. During the early stages of development when no sales are being made but substantial expenses are being incurred, the company would be showing large losses. Later, as large revenues are generated, but proportionately smaller expenses are being incurred, the company would be generating very large profits. In other words 'program accounting' allows aviation companies to average out the development costs and profits of a new product which has a multi-year development and production cycle.

In the case of Canadair, these capitalized assets (or deferred expenses) were never expensed and matched against revenues because management announced on 7 June 1983 that a 'sufficient level of sales could not be made to recover the capitalized costs.'[76] In its 1982 financial statements, Canadair decided to write off $1,054,327,000 of capitalized costs. In addition, Canadair reported a loss for the 1982 fiscal year of $350,569,000. The effect was a net loss for 1982 of $1,414,896,000 compared to a 1981 profit of $3,035,000.

In addition to the inventory work-in-progress writeoff, Canadair's 1982 notes stated that the company would no longer be capitalizing certain development costs such as finance, marketing, product support and general and administrative expenses.[77]

Senator Austin's report on Canadair has blamed management, slow sales, monthly interest payments of $12.5 million and obligations to suppliers for parts the company did not need for Canadair's troubles. He assigned to the CDIC the task of monitoring the company and of determining whether Canadair can become profitable with a new business plan.[78]

The political debate

Debate on Canadair centred on the absence of effective government control over the company's actions in both the inadequacy of financial reporting methods and the lack of adequate management by the board of directors.

Kenneth Dye, Auditor-General, in the media and in the House of Commons Committee hearings pointed to a serious absence of controls over Canadair. Don Blenkarn quoted Dye's statement that, 'what we have here is a costly experiment about which Parliament and the people received little relevant and realistic information ... Bills C-153 on

Crown Corporations and C-158 on CDIC legislation do not go far enough to avoid a repetition of this tragic affair'.[79] The accountability framework for Canadair was not clear since it is not a corporation covered by the Financial Administration Act. Dye wanted the committee hearings on Canadair to 'tell us about what went wrong in the past [and] more important . . . [to] give us an idea of what we have to do to prevent a similar occurrence in the future.'[80]

During the Public Accounts Committee meetings, Kenneth Dye was asked if there was any early warning system that would have identified Canadair's problems. Mr. Dye stated that the 1982 financial reports were the first Canadair reports tabled before Parliament. Canadair replied that the financial statements are filed with two government agencies, the Department of Industry, Trade and Commerce and the Department of Consumer and Corporate Affairs. The company, however, was vague about how many statements had been sent to the Auditor-General. The Auditor-General also elaborated on his analysis of Canadair's statements. Mr. Dye stated that the largest item in the financial statements that had built up quickly was work-in-process and 'any auditor would concentrate on that and question every element in it'. From 1976 to 1982, the Contracts in Process and Inventories Account went from \$31,966,000 to \$1,031,619,000 (see again Appendices I-IV).

The House of Commons Standing Committee on Public Accounts in its Twenty-Second Report (the Canadair Report), tabled in Parliament in late summer 1983 was highly critical of the role of responsible ministers (lack of detailed information on the company, lack of policy directives, lack of regular disclosure to Parliament), inadequate accountability by the company, inadequate monitoring by the directors of management and excessive use of letters of comfort with no public disclosure.

Canadair's board of directors has received much of the blame for Canadair's escalating difficulties because of its alleged failure to be attentive to Canadair's problems and to warn the government. A 1977 Privy Council Office policy paper states that board members are 'clearly responsible' for the business and affairs of the corporation.[81] In a government position paper, 'Crown Corporations – Direction, Control and Accountability', it is stated that 'directors shall manage the business and affairs of [the] corporation'. In his report on Canadair, Senator Austin concluded, however, that the board of directors of crown corporations sometimes fail to provide the checks and balances they should because of the undue influence accorded to government representatives.[82] Austin

expressed concern about a situation in which government officials were appointed to the board without possessing a great deal of business knowledge and, instead of using their influence to check company actions, assumed that management is acting correctly. In the case of Canadair, board members appear to have held the opinion that their role in company decisions was passive. This is confirmed by testimony from certain board members (none of whom had experience in the aviation industry) before the Standing Committee on Public Accounts of the House of Commons and in public statements.

Assistant Deputy Minister of ITC, A.M. Guerin, while a member of the board from 5 January 1976 to September 1981 and now vice-president CL-215 sales, Canadair Ltd., stated that he perceived it as his role 'to ensure that we had a viable enterprise and to take all steps to ensure that that happened'. He did not believe that he or his staff were 'fully equipped to do second-guessing on management [sales] projections'.[83] Jean-Pierre Goyer, a former Liberal cabinet minister and a member of the board has expressed the same sentiment. However, he claims he took his cues from the government representatives on the board.[84]

Board members relied to a great extent on the 1981 interdepartmental task force[85] and on the reports of the senior review committee established in 1976 for their information. The review committee reported to Guerin and published quarterly reports. The task force incorporated both the review committee and outside experts such as Aviation Planning Services which was brought in for expert advice on Canadair's market outlook, particularly with regard to the Challenger.

Public-sector board members such as Mr. Guerin, William Teschke (formerly Secretary, Ministry of State for Economic Development, member of the board from 14 September 1981 to 3 February 1982), and Gordon Ritchie (Associate Deputy Minister, Department of ITC, member of the board from 12 February 1982 to 31 December 1982)[86] conceived a limited role for themselves. Teschke stated that his responsibility was to supplement the task force information to the Minister of ITC, Herb Gray, and to keep the Minister informed. He stated that he did not believe that the report indicated Canadair could not achieve break-even sales (defined as recoverability of inventory), although he did express concerns 'over the ever-escalating peak financial requirements of the corporation'. Public-sector board members all consulted with the Minister prior to meetings and 'attempted forcefully and competently to communicate the concerns of the government to the members of the Board of Directors. . . .'

However, no written instructions were given on the government's position that they were to take to the board. Although the board began to be aware of problems, such as in the Challenger's design, by 1979, Guerin stated that when there were difficulties, management always presented a way of solving them.[87] It was therefore unnecessary to use independent consultants when problems were discovered. Guerin added that he did not feel that the board deferred to his judgements as a government representative.

Private-sector board members appear also to have acquiesced with management. Guy Desmarais, president of Geoffrion, Leclerc Ltd., stated that board decisions reflected optimism on the part of government and management.[88] According to Desmarais, the board and its audit committee believed that the Challenger's break-even level could still be reached since industry experience in previous recessions had shown that corporate jets were effectively recession-proof. Only when executive jets became a luxury and corporations cut costs did the board begin to perceive serious difficulties.

Despite evidence that the board was less than aggressive in pursing its mandate, and despite Senator Austin's inclination to blame it for many of Canadair's problems, the twelve-man board of Canadair was reappointed by the CDIC on 10 June 1983 without a public announcement. The reasoning advanced for this decision was that it would be unfair to change the board's composition since this would be perceived as blaming one or more of the directors.[89]

The policy decision

In November 1982 Canadair was transferred to the CDIC and in June 1983 it was granted the further $240 million in equity that the CDIC had requested. Both decisions were made with a stated belief in the Challenger as a viable project that must continue.

The national unemployment rate had an impact on the decision to assist Canadair. The Montreal area where Canadair's plants are located has experienced chronic unemployment since the onset of the recession. A government official has stated, 'there is just no way the government would accept the death of the Challenger program and all the jobs in Quebec which it provides, both directly and indirectly . . . .'[90] Nevertheless, in public statements of the rationale behind past and future aid

to the company the government has emphasized its export potential and its high-technology importance as well as the employment factors.

Austin has reported that the Challenger 601 is now meeting its promised specifications and the market is recovering although the company has been hurt by adverse publicity.[91] In addition, most development expenses have been undertaken. Termination costs of the program would have exceeded the $240 million requested. These would have involved severance pay and payments to suppliers. Without the additional funds Canadair would have failed by the fall of 1983 and the money would have to be spent even if no more Challengers were produced.

POLITICAL IMPLICATIONS

Senator Austin cited poor management decisions and a lack of communication among board members as major factors in Canadair's difficulties. The transfer of the company to the CDIC is intended to bring the company to surer ground.[92]

The CDIC's primary functions will be to act as a central forum to review the government's commerical investments and institutionalize the government's role as equity banker for ailing large corporations. It is intended to

> replace ad hoc responses to corporate crises with a systematic regime intended to avoid unnecessary long-term commitments of capital . . . [and to act] as a vehicle for the competitive rehabilitation of firms experiencing financial difficulties in anticipation of eventual partial or complete privatization.[93]

The CDIC has the power to invest in any sector of the economy with cabinet approval. This has been a source of criticism because the CDIC may sell off its holdings and retain any profit rather than turning it over to the Consolidated Revenue Fund.

In the future Canadair will be controlled by the CDIC to whom it must pay management fees.[94] Canadair's long-term debt has been transferred to the CDIC's books to free the company of responsibility for $150 million per year in interest payments.[95] Most of the debt is guaranteed by the government of Canada.[96] CDIC will use a 'pool of revenue' from its subsidiaries (Teleglobe Canada for example), its $3 billion in borrowing

authority, and $1 billion equity to help finance Canadair's expenses. It will be monitored by cabinet through the presentation of quarterly earnings for itself and its subsidiaries, and by Parliament through the presentation of annual reports.

The accountability of the CDIC has itself stimulated extensive political debate. Although Pierre Bussières, Minister of National Revenue, has stated that 'it will provide for a regular and constant presence of the government as shareholder to safeguard the interests of all Canadians and provide stricter management of Canadair as well as more realistic market expectations',[97] this view is not without critics. The CDIC and its subsidiaries (such as Canadair) are not subject to the Financial Administration Act, and their accounts are not audited by the Auditor-General (a situation which Kenneth Dye has strongly criticized in debates on CDIC legislation). Senator Austin, chairman of the CDIC, has defended it as an efficient manager – a holding company operating at arm's length from Parliament. Austin contends that the CDIC's $3 billion credit line represents a suitable mechanism to ensure the CDIC's accountability.

The transfer of Canadair to the CDIC has affected government structure. Different branches of the Department of Regional and Industrial Expansion monitored the activities of Canadair in 1982, a year of confusion.[98] Through the purchases by Canadair many smaller firms had benefited by the implementation of DRIE's strategy for the aerospace sector. With Canadair no longer reporting to DRIE, a co-ordinated approach to aerospace industrial strategy is difficult. What the CDIC intends for Canadair, and whether it will re-organize the industry awaits the report of its review of the company.

The reaction of business leaders to the transfer of Canadair to CDIC has been negative. Sam Hughes, president of the Canadian Chamber of Commerce, stated that the CDIC will blame all of Canadair's troubles on old management. It will then write off the $350 million in operating losses and $1.054 billion development costs and interest expenses. At this point, the company will appear to be making money and the Liberals will have made a political gain.[99] Max Ward, president of Wardair, and Larry Thibeault, executive vice-president of the Canadian Manufacturers Association echoed these sentiments. Ward claimed it was 'disgusting' that Canadian taxpayers must foot the bill for a plane that is not selling.

On 13 March 1984 the CDIC effectively assumed the debts of Canadair Limited. The company was financially restructured such that CDIC incor-

porated a new subsidiary, New Canadair (to be called Canadair Limited-Canadair Limitée) which assumed the assets and current liabilities of 'old' Canadair. CDIC has asked Parliament for $310 million to make Canadair a 'free standing' business without having to seek annual cash appropriations. The $310 million is part of an overall cash requirement of $433 to meet Canadair's needs to the end of March 1985. The balance will be met through borrowing. Canadair Ltd. is left with no significant assets and $1.35 billion in debt to be repaid as it comes due (in effect, by the government).

Senator Jack Austin, Minister of State responsible for CDIC, stated that the main issue in the restructuring was to find a way to enable Canadair to concentrate on selling planes, and to ensure the marketplace that the company would survive. Two independent market surveys commissioned by the CDIC concluded that Canadair could be profitable, if its accumulated debt was treated as a sunk cost, if it captured 10 to 15 per cent of the world market, the equivalent of producing fifteen planes a year. An analysis of unit costs of production at the rate of fifteen planes a year concluded that the program was feasible.

It was decided by the CDIC and the board and management of Canadair that the compnay's past debt was a barrier to future sales since it resulted in a negative net worth for the company – a characteristic of bankruptcy. Therefore, the debt assumption by the CDIC was an attempt to restore market confidence in Canadair. CDIC will work out debt servicing with the government. In future, CDIC and not Canadair will answer in parliament for the company's debts. Austin's rationale is that the government is responsible through loan guarantees for the debts whether the debt is on the books of Canadair or the CDIC. However, on Canadair's books the debt hurt the company's future while on the CDIC's books it will not harm Canadair.

This conclusion has been disputed by Robert Joedick, an aviation financing specialist at New York's Lehman Brothers Kuhn Loeb Inc. Joedick has stated that government ownership of the company has always assured its future. Instead, corporations have not bought Challengers because the $13 million price tag is too high for executives, while the nineteen-passenger limit is too small for regional airline use. The Challenger 'falls between the markets. It has to redefine its market or else I cannot see things improving.'[100]

A number of remedial steps have been taken to improve the financial and political accountability of Canadair, and to cut operating costs.[101]

The company must present audited annual and unaudited quarterly financial statements to the government and Parliament. Thus, responsible senior officers of CDIC and Canadair can be questioned by the appropriate cabinet and parliamentary committees. CDIC also has four senior deputy ministers on the board of Canadair and their ministers are kept informed so they can deal with underlying policy issues. CDIC discusses policy questions with the government, receives instructions and guidance, and translates these into Canadair's management procedures in the context of traditional operating business standards.

Canadair has adopted a more conservative use of program accounting and has restored the internal audit function. All but two outstanding letters of comfort have been converted to loan guarantees. Senior management and staff have been re-organized and reduced in numbers. By the end of 1983 total employment fell 25 per cent from the 1982 level (and is now at 4,530) which will translate into total overhead savings of $27.5 million per year. The gradual reduction of the production rate to fifteen planes per year resulted in cash savings of $37 million in 1983, and should result in further cash savings of $141 million in 1984. The 1983 loss from operations was $83.8 million, down from $145.1 million in 1982. In 1983 costs were less than sales revenue by $22.5 million whereas in 1982 costs were greater than revenue by $71.6 million. The company now takes a more conservative approach to sales by listing only firm orders which are signed at a price which covers all costs.

Canadair has continued to receive program assistance from the government. In 1983 it received $6.2 million ($38.6 million in 1982) under established programs to finance production programs and equipment acquisitions. In 1983, sales to the government totalled $18.3 million as compared to $42.1 million in 1982. The government also continues to cover a number of loan guarantees (see Appendix VII).

Canadair has also continued to receive government orders and subcontract work. On 25 April 1983 John Roberts, Minister of the Environment, announced that the federal government planned to create a national firefighting fleet and purchase over twenty CL-215 water bombers from Canadair for $147 million over the next four years under the Special Recovery Projects Program.[102] Ottawa would purchase four aircraft for use in the Territories, but would only purchase the remaining sixteen on a one-to-one matching basis with the provinces. On 19 July 1983 it was announced that Quebec and Saskatchewan would each purchase two, Ontario would purchase three, and Newfoundland four.[103]

This brought the total order to twenty-six planes. Canadair needed a large domestic order to continue production of the plane which was claimed to be unique in its capacity for fighting forest fires. However, political opposition was expressed by Conservative MP Pat Carney who alleged that water-bomber planes have been proven to be inappropriate for forest fires in northern Canada.[104] Lakes are often too small and covered with ice for the aircraft to pick up water. Government support of the CL-215 is effectively another bailout which will guarantee at least two more years of production.

Canadair's production of water bombers, military surveillance drones and subassemblies for other aircraft manufacturers appear to be profitable operations (subject to the subsidies implicit in government procurement).[105]

In November 1984 the new Conservative government (elected in September) proposed the sale of CDIC assets. A Treasury Board-Department of Finance group has been studying Crown corporations with the objective of developing a 'privatization' policy. Although CDIC was created in March 1982 to sell certain Crown corporations once they were potentially profitable, any sale of its assets will not be without problems. Immediate issues which arise are the possible implications of foreign ownership and corporate concentration.

Included in CDIC's assets are both Canadair and DeHavilland. Following the restructuring of Canadair and the assumption of its debt by CDIC, the company turned a $961,000 profit in the first six months of 1984 on sales of $232 million[106] (although this profit cost Ottawa approximately $2.1 billion; $1.35 billion in debt assumption and equity infusions). Canadair has recorded sixteen sales in 1984 which will allow the company to reach its break-even level of fifteen orders. Sales to West Germany of six planes have boosted the company's international image. DeHavilland remains a cash drain and is expected to need approximately $400 million in equity infusions in the immediate future.

NOTES

1 The CDIC also holds the Crown's share in DeHavilland Aircraft of Canada Ltd., Eldorado Nuclear Ltd., Teleglobe Canada, 85 per cent of the common stock in the Canada Development Corporation (representing 48.5 per cent of the voting rights), and Ottawa's small

non-voting stake in Massey Ferguson Ltd. (*Financial Post 500* June 1983)

2 A Report by Senator Jack Austin of Canadair Ltd. to the Standing Committee On Public Accounts 7 June 1983. (Ottawa: Minister of State).

3 The nine companies are Canadair, DeHavilland, Pratt and Whitney, SPAR Aerospace, Bristol Aerospace, Litton Systems, Computing Devices and CAE Electronics. From Report of the Aerospace Manufacturing Sector Consultative Task Force 30 June 1978. Chairman D.C. Lowe (Fred Kearns was a member).

4 Exports (Canadair):

Exports as percent of total sales 1982	1981	1982 rank by exports	Total Cdn. exports ($ million)	1982/81 percent change	Rank in FP500 1982
87	80	31	371	+63	160

Toronto Star 14 April 1983

5 *Austin Report*, 12. Of the 3,800 aircraft which Canadair produced from 1943-1974, almost 3,000 were sold to the Canadian government, primarily for military purposes.

6 Grants to Canadair:

	1965/66 to 1969/70	1970/71 to 1974/75 ($)
TIP	nil	39,702.89
DREE	nil	nil
IRAP	prohibited by the Industrial Research and Development Incentives Act to divulge information.	
PAIT	4,601,601[a]	648,400[b]
ESP	n.a.	n.a.
DIR	668,252	1,061,352[e]
DIP	26,184,173[c]	20,505,753[d]

Potentially recoverable to the following extent:

a	$4,601,601
b	648,400
c	19,465,382
d	20,453,686

(*Hansard* 7 May 1975)

e the allotment for 1974-75 which is not an actual expenditure to date has not been included in the total.

7 *Hansard* 22 October 1975.
8 Ibid., 28 November 1975. The contract was worth $950 million.
9 *Canadian Business* December 1978, 75.
10 Austin Report, 12-13.
11 Gordon, Marsha (1982) *Government in Business* (Montreal: C.D. Howe Institute) 84.
12 *Financial Post* 11 January 1975.
13 *Hansard* 7 May 1975.
14 Ibid., 22 October 1975.
15 Ibid., 17 November, 27 November 1975.
16 Austin Report, 15.
17 *Globe and Mail* 3 November 1973, 27 December 1975.
18 *Hansard* 17 May 1976.
19 Austin Report, 15.
20 The government paid $11,479,835 for 1,408,463 shares of Canadair, $25,710,165 for nine outstanding promissory notes of Canadair to General Dynamics and $1,500,000 representing the company's profit in the period 1 January 1974 to 31 December 1975. (*Hansard* 24 January 1977).
21 *Financial Post* 31 November 1976.
22 *Canadian Business* December 1978, 75.
23 Austin Report, 17.
24 *Executive* November 1977.
25 Ibid., 16.
26 *Globe and Mail* 1 November 1976.
27 *Canadian Business* December 1978.
28 *Toronto Star* 8 July 1977.
29 Challenger vs. the competition:

	Fuel consumption (nautical miles)	Speed (long-range)	Range (at max. cruise speed)	Direct operation cost/ mile	Cabin floor area
Challenger	9,870 lbs.	459 kt.	3,900 n.m	$0.93	205.5 sq.ft.
Falcon 50	12,250	437	3,550	1.06	113.2
Gulfstream III	16,304	445	3,600	1.16	207.1

30 *Montreal Gazette* 11 June 1983.
31 *Canadian Aviation* June 1983, 4.
32 *Fifth Estate transcripts* 13 April 1983, 3.
33 Austin Report, 19.
34 *Fifth Estate*, 18.
35 *Toronto Star* 14 April 1983.
36 Ibid.
37 *Montreal Gazette* 11 June 1983.
38 *Hansard* 13 April 1983.
39 *Globe and Mail* 18 April 1983.
40 Ibid., 8 June 1983.
41 Austin Report, 21.
42 Ibid., 22.
43 *Hansard* 1 June and 15 April 1983 – Ian Waddell. Reference to a 15 November 1981 meeting of the House of Commons Finance Committee in which the members were not informed that costs were rising.
44 Austin Report, 23.
45 *Globe and Mail* 5 August, 1983.
46 Employment levels at Canadair:

1974	2,400	*a*	
1975	1,800	*b*	
1981	6,170	*c*	(post-Challenger jet)
1982	6,000	*d*	
Jan/83	5,400	*e*	

SOURCES:
a Austin Report, 12
b *Globe and Mail* 1 November 1976
c *Hansard* 9 February 1981
d *Globe and Mail* 9 August 1982
e *Toronto Star* 9 July 1983

Employment levels after introduction of Challenger jet:

	Male	Female	Total
Age 15 - 24	1192	438	1630
Over 25	4339	201	4540
	5331	639	6170

(188 permanent staff are nonCanadian and 227 subcontract personnel are non-Canadian.)

47 *Globe and Mail* November 1976.

48 *Canadian Business* December 1978. In late 1978 Canadair signed a three-year contract with the IMA.

49 *Montreal Gazette* 27 October and 6 April 1982.

50 *Globe and Mail* 13 April 1983. In April 1983 Canadair laid off 450 workers as of mid-July due to lagging sales of the Challenger. Thirty were to be laid off every month until July when 450 were to be let go.

51 *Montreal Gazette* 7 October 1982.

52 Ibid., 27 October 1982.

53 Minutes of the House of Commons Standing Committee on Public Accounts 21 June 1983, 89:26.

54 *Fifth Estate* transcripts 13 April 1983, 5.

55 *Hansard* 9 December 1982. Fourteen letters of comfort were signed by Herb Gray as Minister of ITC.

56 *Fifth Estate*, 8.

57 *Hansard* 9 December 1982.

58 *Toronto Star* 23 March 1982.

59 Minutes of Proceedings and Evidence of the Standing Committee on Public Accounts 7 June 1983, 85A:11.

60 *Hansard* 2 March and 14 April 1983.

61 *Toronto Star* 23 March 1982.

62 *Globe and Mail* 16 June 1982.

63 *Hansard* 14 April 1983.

64 Ibid.

65 *Fifth Estate* 13 April 1983.

66 *Hansard* 28-29 October 1982.

67 Ibid., 14 April 1983.

68 Ibid.,18 May 1983.

69 Ibid. 26 May 1983.

70 Revenue and sales, 1981-82:

	1982	1981
Revenue	$(360.6m)	$3.0m
Sales	$429.4m	$285.7m

In 1982 Canadair wrote off $1,054,300,000 in unrecoverable inventory costs, in its loss of $1.4 billion, $1 billion was due to the Challenger (*Globe and Mail* 8 June 1983).

71 *Globe and Mail* 18 June 1983.

72 *Toronto Star* 8 June 1983.

73 Since financial statement information is available for Canadair, an Altman bankruptcy prediction model was utilized along with standard financial ratio analysis. The former generates negative Z scores – an indication of financial distress and bankruptcy – from 1978 to 1982 with the largest value by far in 1982. However, the financial accounting practices of the company as described in this section is unique and the resulting financial ratios are difficult to interpret relative to other companies with more standard reporting practices.

74 Minutes of Proceedings and Evidence of the Standing Committee on Public Accounts, 85:19, 7 June 1983.

75 Ibid.

76 Ibid., 85A:11,20-21.

77 Ibid., 85:27.

78 The mandate of the CDIC vis-à-vis Canadair:

1 Developing a business plan.

2 Cut production to reduce cash requirements and avoid inventory buildup.

3 The above necessitated a reduction of the work force by 650 to the end of July 1983.

4 Establish a new elective committee of the board chaired by the President of the CDIC, Joel Bell.

5 Initiate a thorough, technical review of the engineering, cost control, financial reporting and production operations of the company.

6 Independent market appraisals.

7 Past contracts reviewed and some renegotiated – the case involving bribery in Alaska has been referred to law officers of the Canadian Department of Justice to determine if Canadair or its employees committed any wrongdoing.

8 All future transactions must meet the standards of the CDIC.
9 Recruiting a new Chief Exeuctive Officer (Austin Report, 39).

79 *Hansard* 9 June 1983.
80 Public Accounts 14 June 1983, 5.
81 *Globe and Mail* 13 August 1983.
82 Austin Report, 47.
83 Public Accounts, 14 June 1983.
84 *Globe and Mail* 14 June 183.
85 Involved in the Task Force were the Departments of Finance, Treasury Board, Transport, and ITC.
86 Other civil servants were Messrs. Stoner (Deputy Minister, ITC) Burns (Senior Assistant Deputy Minister), Laviguer (Deputy Minister), Troop (Assistant Deputy Minister, Justice).
87 Public Accounts, 21 June, 1983, 89:12.
88 *Toronto Star* 24 June 1983.
89 *Globe and Mail* 3 August 1983, and Public Accounts 21 June 1983. The re-appointed Board was G. Desmarais, Joel Bell, J.P. Goyer, C. Rathgeb, L. Lavoie (CEO of the National Bank of Canada), J.P. Sullivan (lumber), B. Deschenes (Montreal lawyer), Fisher (paper), Milton Harris (Toronto industrialist), Paul Marion (food), D.M. Culver (CEO, Alcan), J. Pepper (Montreal lawyer), G.S. Bennett.
90 *Financial Post* 18 June 1983.
91 Austin Report, 47.
92 Ibid., 43.
93 Brooks, Stephen (1983) 'The state as entrepreneur: from CDC to CDIC'. *Canadian Public Administration* (Winter) 26(4):525-43.
94 *Financial Post* 29 May 1983.
95 *Montreal Gazette* 9 June 1983.
96 Austin Report, 51.
97 Hansard 15 June 1983.
98 *Financial Post* December 1982.
99 *Toronto Star* 8 June 1983.
100 *Macleans* 26 March 1984.
101 See CDIC *Canadian Update*, March 1984 and 'Response of the Government to the Standing Committee on Public Accounts Report on November 17, 1983 with respect to Canadair Ltd.'. Presented by Jack Austin, Minister of State responsible for CDIC.
102 Minister of the Environment Press Release 25 April 1983.

103 *Globe and Mail* 19 July 1983.
104 Ibid., 11 May 1983.
105 CDIC *Canadian Update* March 1984.
106 *Financial Post* 10 November 1984.

APPENDIX I

Canadair Limited consolidated statement of income ($000's)

	1982	1981	1980	1979	1978	1977	1976
Sales	429,379	285,662	116,212	115,630	82,848	60,050	44,594
Expenses including cost of sales, selling, general and administrative expenses, research and development	574,471	279,154	110,895	111,850	79,494	57,782	41,325
Interest and other financing	215,477	3,430	1,733	37	85	793	1,807
	789,948	282,584	112,628	111,887	79,579	58,575	43,132
Income (loss) before unusual items and income taxes	(360,569)	3,078	3,584	3,743	3,269	1,475	1,462
Unusual items relating to the Challenger program	(1,054,327)	–	–	–	–	–	–
Income taxes	26	43	52	60	40	54	642
Net income (loss)	(1,414,922)	3,035	3,532	3,683	3,229	1,421	820
Extraordinary loss	–	–	–	–	–	–	(1,373)
Tax reduction	–	–	–	–	–	35	638
Net income (loss)	(1,414,922)	3,035	3,532	3,683	3,229	1,456	85

APPENDIX II

Canadair Limited consolidated balance sheet – assets ($000's)

Current assets	1982	1981	1980	1979	1978	1977	1976
Cash	5,497	3,012	3,671	3,294	543	666	191
Accounts receivable	43,045	65,516	41,544	13,058	8,948	12,707	16,587
Contracts in process and inventories, less advances and progress billings	127,651	1,031,619	594,120	376,961	210,973	71,157	31,966
Prepaid expenses	5,040	3,322	1,737	1,622	729	702	430
	181,233	1,103,469	641,072	394,935	221,193	85,232	49,174
Property, plant, and equipment (net)	58,179	55,801	54,720	33,152	23,008	19,162	18,254
Long-term receivables	5,129	–	–	–	72	213	362
Deferred charges	22,483	(1,443)	1,558	1,951	2,252	–	–
Total	267,024	1,157,827	697,350	430,038	246,525	104,607	67,790

NOTE: Canadair's 1982 financial statements reflect a writedown in the value of inventory relating to the Challenger program.

APPENDIX III

Canadair Limited consolidated balance sheet – liabilities ($000's)

	1982	1981	1980	1979	1978	1977	1976
Current liabilities							
Bank loan	10,575	322,087	257,009	127,305	78,490	40,385	14,400
Accounts payable and accrued liabilities	352,949	117,019	118,608	68,449	39,963	23,056	10,647
Customer deposits	2,620	13,186	48,798	17,201	–	–	3,017
Income and other taxes	–	–	–	24	17	87	48
Principal due within one year on long-term debt	86,062	50,212	2,656	1,041	175	55	55
	452,206	502,504	427,071	214,020	118,645	63,583	28,167
Long-term debt	975,605	601,160	218,990	168,261	83,744	95	150
Shareholders' equity							
Capital stock							
Preferred shares - Class B	25,170	25,170	25,170	25,170	25,170	25,170	25,170
Common shares - Class A	17,244	17,244	17,244	17,244	17,244	17,244	17,244
	42,414	42,414	42,414	42,414	42,414	42,414	42,414
Contributed surplus	200,000	–	–	–	–	–	–
Excess of appraised value of land over cost	10,760	10,788	10,949	10,949	11,011	11,033	11,033
Retained earnings (deficit)	(1,413,961)	961	(2,074)	(5,606)	(9,289)	(12,518)	(13,974)
	(1,160,787)	54,163	51,289	47,757	44,136	40,929	39,473
Total liabilities & shareholders' equity	267,024	1,157,827	697,350	430,038	246,525	104,607	67,790

NOTE: Canadair's 1982 financial statements reflect a writedown in the value of inventory relating to the Challenger program.

APPENDIX IV

Canadair Limited consolidated statement of changes in financial position ($000s)

	1982	1981	1980	1979	1978	1977	1976
Working capital derived from							
Net income (loss)	(1,414,922)	3,035	3,532	3,683	3,229	1,421	820
Loss on discontinued operations	–	–	–	–	–	–	(385)
Depreciation	6,126	5,084	5,576	4,196	2,144	1,407	1,330
Reduction of long-term receivables	–	–	–	72	141	149	189
Amortization of deferred charges	11,981	570	568	551	295	–	–
Extraordinary item	–	–	–	–	–	35	204
Long-term debt, net of discount & expenses	620,087	434,025	52,972	85,308	81,277	–	–
Consolidated surplus	200,000	–	–	–	–	–	–
Subscription of shares	–	–	–	–	–	–	8,469
	(576,728)	442,714	62,648	93,810	87,086	3,012	10,627
Working capital applied to							
Additions to property, plant & equip't (net)	8,532	6,326	27,144	14,402	6,012	2,315	82
Reduction on long-term debt	255,086	51,886	2,418	1,041	175	55	55
Long-term receivables	5,129	–	–	–	–	–	–
Increase (decrease) in deferred charges	26,463	(2,462)	–	–	–	–	–
	295,210	55,750	29,562	15,443	6,187	2,370	137
Increase (decrease) in working capital	(871,938)	386,964	33,086	78,367	80,899	642	10,490
Working capital at beginning of year	600,965	214,001	180,915	102,548	21,649	21,007	10,517
Working capital (deficiency) at end of year	(270,973)	600,965	214,001	180,915	102,548	21,649	21,007

NOTE: Canadair's 1982 financial statements reflect a writedown in the value of inventory relating to the Challenger Program.

APPENDIX V

Challenger sales and break-even forecasts

	October 76	October 79	March 80	December 80	June 81	December 82
Estimated sales						
CL-600	250	250	202	220	201	144
CL-601	–	–	71	58	126	275
CL-610	–	–	150	148	179	–
Total Challengers	250	250	423	426	506	419
Target date for production	84:1	84:2	86:4	87:4	88:4	93:4
Break-even quantity	136	185	255	298	349	389
Achievement of break-even	82:1	83:2	84:2	85:4	86:4	92:4

APPENDIX VI

Challenger program source of funds, 1976-83 ($000's)

	31 December						
	1976	1977	1978	1979	1980	1981	1982[a]
Sales proceeds and advances from customers	7,843	24,326	41,796	96,798	223,881	369,153	634,994
Equity injection	–	–	–	–	–	–	200,000
Bank loans	–	40,385	78,490	127,305	257,009	322,087	10,575
Long-term debt	–	150	83,919	169,302	221,646	651,372	1,061,667
Other[b]	(3,016)	7,025	23,021	43,282	61,880	(33,328)	41,905
	4,827	71,886	227,226	436,687	764,416	1,309,284	1,949,141

a Prior to adjustments for Challenger unusual items at 31 December 1982.

b Includes funds provided from changes in other balance sheet items.

Figures are cumulative.

SOURCE: Austin Report, 7 June 1983.

APPENDIX VII
Canadair Limited, notes to consolidated financial statements (continued), year ended 31 December 1983 ($000s)

Long-term debt	1983	1982
Loans covered by government of Canada guarantee or other government support:		
Notes due 15 June 1983 with interest at 8.5% (US $70 million)	$ –	$ 86,058
Term loan due 4 October 1984 with interest at 9.75% (US $30 million)	37,332	36,882
Term bank loan due 14 January 1985 with interest at one year LIBOR plus 7/8% renewed annually and annual payments of principal of US $1.25 million (US $22.5 million) (note 7)	–	27,662
Term loan due 22 August 1985 with interest at 9.75% (US $10 million)	12,444	12,294
Term bank loan due 7 May 1986 with interest at LIBOR plus 0.5% (US $187.5 million) (note 7)	233,325	230,513
Term loan due 1 December 1986 with interest at LIBOR plus 3/8% (US $75 million)	93,330	92,205
Term notes due 15 March 1987 with interest at 15.5%, callable after 15 March 1985 at 101% of principal amount; 100.5% after 15 March 1986 (US $150 million)	186,660	184,410
Notes due 1 June 1984 with interest at 16 3/8% (US $50 million)	62,220	61,470
Term bank loan due 11 November 1988 with interest at LIBOR plus 3/8% or US prime rate, revolving to 11 November 1986 with payments equal to 25% of the outstanding balance commencing from 11 May 1987 and continuing semi-annually until maturity (US $60 million) (note 7)	74,664	61,470
Carried forward	$699,975	$792,964

APPENDIX VII (continued)

Long-term debt	1983	1982
Brought forward	$ 699,975	$ 792,964
Syndicated term loan due 6 March 1989, with interest at LIBOR plus 3/8% or US prime rate to 12 March 1985 and LIBOR plus 0.5% or US prime rate plus 1/8% thereafter, revolving to 6 March 1987, with payments equal to 25% of the outstanding balance commencing from 6 September 1987 and continuing semi-annually until maturity (US $50 million)	62,220	122,940
Notes due 15 November 1989 with interest at 12.5%, callable at a maximum of 105% of principal amount (US $175 million)	217,770	215,145
Term loans due 22 March 1992 with interest at prime rate less 0.75%, revolving until 22 March 1987 and continuing semi-annually with the balance repayable at maturity	42,444	20,000
Term loan due 22 March 1992 with interest at prime rate less 0.75%, with payments equal to $5 million commencing from 22 March 1988 and continuing semi-annually with the balance repayable at maturity	100,000	–
Discounted note due 26 April 1992 with interest at 8.5%$ (US $30 million)	37,332	36,882
Less unamortized discount on issuance of long-term debt	(10,455)	(11,741)
Total	$1,149,286	$1,176,190

4
White Farm Equipment Canada Ltd.

INTRODUCTION

White Farm Equipment Canada was founded during White Motor Corporation's expansion-by-acquisition program in the 1960s. The Brantford plant was purchased from Cockshutt Farm Equipment in February 1962 to complement the 1960 purchase of the Oliver Corporation (Chicago). White had no previous involvement in the manufacture and distribution of farm equipment, but had operated bus and truck facilities in Canada since 1916.

In the early 1970s, White US experienced management and financial difficulties and sold many of its holdings. When White went into receivership in 1980, White Canada also applied for court protection. In 1981 the Canadian truck and farm-equipment assets were sold. Two new Canadian-controlled companies emerged: White Western Star Trucks Inc. of Mississauga, Ontario and Kelowna, BC, and White Farm Equipment Canada of Brantford, Ontario. In order to keep the Brantford plant operating and in Canadian hands, the new owners received substantial government financial assistance. (The terms 'loan insurance' and 'loan guarantees' are often confused. 'Guarantee' is used to refer to either or both types of assistance in this case.)

In 1982 White Farm was taken over by its 49.9 per cent American shareholder, TIC Investments Ltd. When the 1982 season was unprofitable and the new owner failed to meet its debt obligations, secured creditors withdrew their financial support. White Farm was in receivership from June 1983 until January 1984. The new owner, Bill Sinclair of Oakville, also purchased the White Credit Corporation of Canada.

COMPANY BACKGROUND

The full history of White Farm and related companies is presented in the Appendix 4A chronology. The founder of the Brantford farm-equipment manufacturing facilities now known as White Farm Equipment Canada Ltd. was the White Motor Company of Cleveland, Ohio. White Motor was incorporated in 1900 and was originally involved in the manufacture of trucks and buses in the United States. White trucks were first sold in Canada in 1909 and the White Motor Company of Canada Ltd. was incorporated in 1916.[1]

In April 1929, White Canada became a separate region dealing directly with the head office in Cleveland. It had previously been grouped with all non-US subsidiaries in the parent firm's 'export' region. This change was made in response to rapid growth in Canadian sales.[2] White Canada opened its first production facilities in Montreal on 1 June 1931.[3] This plant was used to modify trucks and buses for the Canadian market.[4]

In the late 1940s, White Canada issued first-mortgage bonds (guaranteed by White Motor) and constructed a $2.5 million plant in Montreal.[5] Canadian branch operations were expanded and local sales and service organizations improved.[6] In 1950 White added buses to its Canadian output under an agreement with Flexible Co. of Loudonville, Ohio.[7] The Montreal plant was closed in 1954 for economic reasons.[8]

In the late 1950s Canadian truck sales grew rapidly. White Canada moved its Canadian headquarters to Toronto and invested $2 million in further expansion of its sales and service centres.[9] In 1961 White sold over $20 million worth of trucks in Canada. Market growth and the development of parts and materials suppliers prompted a return to domestic manufacturing. A $1-million truck plant was opened in Brantford in the autumn of 1962.[10] On the west coast, White agreed in 1961 to sell and service the truck products of Freightliner of Canada Ltd. (Vancouver).[11]

In the early 1960s, White also became involved in the manufacture of farm equipment. White acquired the Oliver Corporation, a Chicago farm-implement firm, in 1960.[12] Canadian distribution was handled by the Oliver Corporation of Canada. In 1961, Oliver had total sales of $70 million but only $3.5 million in Canada. To increase market penetration and provide Canadian manufacturing facilities, White acquired the Cockshutt Farm Equipment Company, Brantford, in 1962. Cockshutt

had 750 Canadian and 150 US dealers.[13] The new truck plant was built adjacent to the Cockshutt plant in Brantford, in a former steel warehouse purchased from CKP Investments Ltd.[14] Truck engines were supplied by Cummins Diesel of Canada Ltd., the Canadian sales subsidiary of the Cummins Engine company. White and Cummins merged in 1963.[15]

In 1966, White selected Kelowna, BC as the site for a new $4 million 'White Western Star' truck plant. Kelowna offered inexpensive industrial land and tax concessions. Further tax savings were available through accelerated depreciation since Kelowna was a federally designated low-growth area. Kelowna was to be transformed from a one-industry town (Okanagan fruit) to a diversified centre.[16] White executives stated that the decision to locate in Western Canada was a direct result of the Canada-US Auto Pact.[17]

In the 1960s the White Motor Corporation grew rapidly through acquisitions. It purchased Oliver, Minneapolis-Moline and Cockshutt in farm equipment, Hercules, Superior and Alco in engines, Reo, Diamond and Autocar in trucks and Euclid in construction equipment. White's acquisitions were often financed through the exchange of shares, so the large number of acquisitions did not drain corporate cash flows. However, the operations of the new subsidiaries significantly increased the company's need for working capital and this proved to be a serious problem. In 1969, the strain on corporate resources started to translate into reduced profitability. Dividends exceeded earnings in the final quarter of 1969. At that time, White was the 270th largest US corporation with annual sales of $750 million.[18]

The 1970s

White Motor floundered in the 1970s, with questionable strategies and bad luck. White raised funds through increased borrowing. Cash-flow shortages were also reduced by the sale of profitable holdings which had large working-capital requirements.

One major investment was the replacement of the outdated Cleveland plant with a more modern version in Roanoke, Va. It came into production just before a sharp downturn in the North American truck market in 1980. Millions were invested to develop a truck diesel engine for White's new Canton, Ohio plant. Funds were not available to bring the plant into operation and it took several years to sell it. In trucks, White altered its strategy and produced increasingly standardized

vehicles. This threw White's products into head-on competition with GM, Ford and International Harvester. It was difficult to compete for fleet orders on the basis of price, and sales suffered. When the Cleveland plant was closed, corporate headquarters were moved to Farmington Hills, Michigan.[19]

Problems at the parent company left White Canada with frequent management changes. It had four presidents in the 1970s and management was made even more difficult by White Motor's desire to sell the North American farm-equipment business.[20] White Western Star trucks remained very profitable, producing custom-made trucks in a small plant. Its major competitive advantage was short delivery times.[21] When truck sales dropped off generally in 1980, the Kelowna plant outperformed its competitors under the direction of general manager William Tigg. He raised the plant's productivity through production-line changes, upgraded quality control and made changes in materials handling and scheduling.[22]

At the Brantford farm-equipment plant, White continued to spend money on research and development despite financial problems. The model 9700 axial-flow combine, developed with federal government assistance, was the plant's best opportunity to improve market share. This product laid the foundation for the new company formed later.[23]

In the late 1970s, White Motor was unable to arrange long-term financing and relied on 164-day revolving credit arrangements. On 26 August 1977 a new agreement was reached with Canadian and US banks providing over $300 million of further revolving credit. Of this amount, $92.9 million was allocated to the parent company on a two-year basis and $201.9 million to the finance subsidiary, White Motor Credit Corporation. Some $43.9 million of the credit corporation's funds were to be used to finance Canadian operations. The White Motor Credit Corporation of Canada Ltd. finances wholesale and retail sales contracts for White's products sold in Canada.[24]

On 6 September 1979 White Motor exchanged 1,050,000 common shares for 126,138, $6.75 cumulative preferred series A shares which were held by subsidiaries of Studebaker-Worthington. The preferred shares were issued in 1969 when White bought Alco engines from Studebaker-Worthington. Dividends were omitted after 1975 and scheduled redemptions were not made after 1976 due to White's restrictive debt arrangements. The preferred shareholders obtained their common shares after bringing a lawsuit against White.[25]

White's financial position deteriorated, as shown in the 1975-78 financial statistics in Table 17. The farm business was unprofitable throughout the 1970s. White Motor first reported operating losses of $324,000 in the first seven months of 1980.[26]

1980: White Motor US goes bankrupt

In August 1980 the Brantford plant was closed due to low farm-equipment sales. Over 1,000 workers were laid off.[27] White Motor US was plagued by a decline in both US truck and farm-equipment sales.[28] Two Cleveland banks seized some of White's assets and the company filed for court protection under Chapter 11 of the US Bankruptcy Act.[29] Announcement of the filing came two days after the expiration of White's 364-day revolving-credit agreement with twenty-seven US banks. Unlike typical financing arrangements in Canada, the US banks were all unsecured creditors. The banks called $77.2 million in loans after White refused to provide them with security. White included its Canadian subsidiary in the 4 September application for court protection. The Canadian plants were expected to continue to operate, supply dealers with equipment and parts and pay employee salaries while the financing problems were worked out.[30]

It was subsequently determined that US proceedings had no legal effect in Canada. On 12 September, White Canada made a proposal to creditors and applied to the Ontario Supreme Court to appoint Clarkson Co. Ltd. of Toronto as interim receiver. A temporary moratorium on the claims of White Canada's creditors was required, as liquidity problems would arise because of relationships with other companies in the group.[31] White Canada had no cash of its own and the parent company's accounts payable were frozen. Canadian operations were financially healthy, but US proceedings caused an interruption in the financing of day-to-day operations.[32] Four hundred White Western Star assembly workers were laid off on 9 September. They were recalled by Clarkson only ten days later.[33]

White Canada executives stated that interim receivership was necessary to protect the claims of Canadian creditors.[34] A $6-million claim by White US was subordinated to creditor's claims. As of September 1980 White Canada had $143.48 million in assets and $67.67 million in liabilities with 1,000 Canadian and 2,000 American creditors.[35] Despite over $75 million in equity, White Canada's future was in doubt as its

TABLE 17
White Motor selected financial information (in $000)

	1978	1977	1976	1975
Total assets	120,521	97,676	91,169	91,135
Sales	299,415	268,443	272,130	244,842
Net income	6,492	5,259	8,740	6,423
Return on assets	5.4%	5.4%	9.6%	7.1%
Profit margin	2.2%	2.0%	3.2%	2.6%

SOURCE: White Motor financial statements.

'banker', its largest supplier, and its largest customer (each being the parent company) were all insolvent at the same time. A contingent liability of $4.5 million, settled two and a half years later, was the UAW claim against White for inadequate notice of layoff at the Brantford plant.[36] White Motor Credit Corporation of Canada was not included in the Canadian interim receivership. Creditors agreed that it should continue uninterrupted. Smaller Canadian White operations, such as parts depots and company-owned dealerships, continued 'business as usual'.

The 12 September proposal to creditors requested a debt moratorium until 31 January 1981.[37] The first creditor's meeting was held in early October. A team of five inspectors was elected and several alterations to the original proposal were negotiated. The date for presentation of the re-organization plan was moved forward to 15 December, with provision for further extensions to 30 April 1981. Creditors insisted that they be consulted and their approval sought for any trustee's actions outside of normal day-to-day operations. The trustee was prohibited from borrowing any substantial portion of the $25 million authorized by the Ontario Supreme Court without creditor approval. Creditors were assured that re-organization as a going concern would permit full recovery of their claims. In the event of bankruptcy, they were warned that off-balance-sheet liabilities would dilute their claims to about 60¢ on the dollar. These liabilities included unfunded pension-plan costs ($20 million), warranty claims ($10 million) and $6 million owed to dealers under a floor-plan financing commitment.[38]

SALE OF WHITE CANADA

Overview

The White Motor Company of Canada Ltd. was sold as two separate units. Canadians acquired all of the Kelowna truck plant and 50.1 per cent ownership of the Brantford farm-equipment plant. It is the Brantford plant which was renamed White Farm Equipment Canada Ltd. after the transactions were completed. The sales required the approval of White US, US and Canadian bankruptcy courts, US and Canadian creditors and the Ontario and federal governments.

Negotiations and interim receivership for White Canada lasted from September 1980 until the end of March 1981. There were several delays due to the number of interested parties and the international nature of the transactions. An outline of the differences between Canadian and US bankruptcy legislation is presented in Appendix 4B.

The sale of White Canada is primarily of interest in that it gave rise to White Farm Equipment Canada Ltd., the subject of this paper. The next section is a brief outline of the sale of the Kelowna plant. This is followed by a description of the sale of the Brantford farm-equipment plant. The complex negotiations which preceded these final outcomes are then presented.

The Kelowna plant

The Bow Valley and Nova corporations, both Calgary-based energy companies, began contemplating the purchase of the White Western Star plant in July 1980. They saw the plant as a 'stand alone business with excellent dealerships, a secure labour force and excellent manufacturing techniques'. At that time the plant supplied 17 per cent of the Canadian heavy-truck market and was exporting 40 per cent of its output to the United States.[39]

On 9 December, Bow Valley and Nova announced a joint takeover offer for White Motor of Canada. These companies intended to operate the Kelowna truck sales and assembly businesses while selling the Brantford farm-equipment plant to a third party.[40] By 15 January, White US had several offers for the Kelowna plant. Other bidders included Consolidated Freightways and Daimler-Benz AG.[41]

On 13 March 1981 the US Bankruptcy Court approved the sale of the truck plant and its dealerships to Bow Valley and Nova's joint company,

259374 Alberta Ltd., for about $30 million.[42] The sale produced Canada's only wholly owned truck manufacturer, White Western Trucks Inc., with 900 employees at the Kelowna plant and corporate headquarters in Mississauga, Ontario.[43] One article claimed that it was 'in dispute' whether White US willingly sold the money-making Canadian truck operations. One-fifth of White's $1.2 billion in sales was from this source.[44] An agreement was reached to ensure that White Motor would continue to buy Western Stars and to supply cabs, other parts and trucks that made up 30 per cent of Canadian sales.[45]

The Brantford plant

On 19 November 1980, TIC Investments Corporation of Dallas Texas, a privately owned holding company, purchased the US farm-equipment business of White Motor. TIC also made an offer to White US for the Brantford plant in November, but the sale was reportedly blocked by FIRA.[46] Another bid came later from Linamar Machine Ltd. of Guelph, a precision machine works. Linamar president, Mr. Hasenfratz, knew the potential of the Brantford plant as he had followed the development of the model 9700 axial-flow combine and supplied some of the parts.[47] It was for the US Bankruptcy Court in Cleveland to choose among these and other bidders.

On 13 March 1981 the US court instructed TIC and Linamar to 'hammer out a partnership'. US creditors had favoured TIC's bid while Canadian creditors favoured the Linamar bid.[48] Linamar took 50.1 per cent to achieve Canadian control. This allowed the new partners to obtain financial assistance from the Canadian and Ontario governments. The assistance package had previously been offered to a Canadian consortium, of which Linamar had been a member.[49] The purchase price was announced 16 March at $4.5 million. The Ontario court and creditors approved the sale on 18 March.[50]

FIRA approved the TIC-Linamar offer on 30 March 1981. Industry, Trade and Commerce Minister Herb Gray announced that several features of the transaction were of 'significant benefit', including the following:

- Former foreign ownership, now over 50 per cent Canadian control.
- Immediate re-activation of the Brantford facilities.
- All 1,100 workers are expected to be recalled by mid-1982.

– Maintenance of R&D facilities in Brantford.
– Maintenance of the existing dealer network plus all dealers to be offered the opportunity to distribute US-built tractors.
– Corresponding US distribution agreement for Canadian-built combines should allow 50 per cent of Brantford production to be exported.[51]

TIC and Linamar paid $1 million for the shares of White, put up $3 million in new equity and reportedly raised $20.3 million in loans, most of which were guaranteed or insured by the federal government and the province of Ontario. At the last minute, banking arrangements had to be changed. The Bank of Montreal had been approached during the negotiations but would not arrange financing. The Royal Bank and Roynat Ltd. (a financial institution specializing in small businesses, of which the Royal Bank is a shareholder) agreed to take on an effective commercial risk of $0.5 million only after the buyers put in another $0.5 million in equity and Ottawa and Queen's Park offered an additional $7 million in loan guarantees.[52] The Borg-Warner Acceptance Corporation of Chicago provided mutual financing for the shared distribution operations.[53]

UAW contract provisions were not a condition of the sale. On 21 March the new White owners asked the union to take a pay cut. The previous three-year contract had been signed in May 1980 and gave hourly employees an average wage of $9.50 per hour.[54] The Brantford workers ratified a new three-year contract on 30 March. Sacrifices included a scaled-down workforce, the suspension until 1983 of payments to the employee's supplementary unemployment benefit fund, no scheduled shutdown (holiday) in 1981 and the deferral of vacation bonuses and paid holidays for 1981 and 1982 until 1983. The workers also won a wage increase of 3 per cent each year plus a cost of living allowance of one cent per hour for each 0.26 per cent rise in the CPI.[55]

Highlights of the negotiations

It was Terry Godsall, the president of Shieldings Investments Ltd., who first recognized the opportunity for Canadian investors in the financial difficulties of White Motor US. In previous undertakings, Shieldings had taken advantage of opportunities created by both the weak American economy and FIRA. When large US companies changed ownership, Canadian operations tended to become available because FIRA was seen as a nuisance.[56]

Godsall first 'sold' Bow Valley and Nova on the Kelowna plant, but realized that a buyer would have to be found for the Canadian farm operations. Nova and Bow Valley were concerned that if White US sold its farm division, it could re-organize its North American truck business and they would not be able to buy the Kelowna plant. To improve their chances, they developed a 'linked-deal' strategy whereby prospective farm-division purchasers were asked to link their offers to a sale of the Canadian truck business to Bow Valley and Nova. Godsall played a 'pivotal role' in pulling together another Canadian consortium, including Shieldings, Linamar and a Canadian employee group.[57] White Farm Equipment president, Andrew Zaleski, was fired by White US for taking part in the bid. He was later re-instated by the new owners.[58] Godsall is also said to have persuaded the two levels of government to offer loan guarantees and insurance to the Canadian consortium. He enlisted the support of federal Industry Department official, David Dodd.[59]

On 2 March 1981, ITC minister Herb Gray announced that the Enterprise Development Board would insure $10.5 million in loans in support of the Canadian consortium. Larry Grossman, Ontario Minister of Industry and Trade and Tourism, announced that the Ontario government would offer the group a $2 million loan and a $3 million loan guarantee. The total government-assistance package amounted to $15.5 million. Further government support for the Canadian bidders came in public statements that FIRA would be unlikely to approve a sale to foreigners, given the existence of alternative Canadian purchasers.[60] On the other hand, the Canadians would have to either fill out the product line in Brantford or negotiate a deal for importing other White equipment. TIC, the new owner of White's US farm-equipment operations, had promised US creditors that should its bid be accepted, a $22-million debt owed to the Canadian operation would be forgiven.[61] The Canadian governments feared that TIC would not re-open the Brantford plant. There was also concern that the combine technology developed with the help of federal R&D grants would be lost to Canada if TIC transferred production to the United States.[62]

While negotiations continued, White dealers and creditors became increasingly concerned. Farm-equipment dealers were concerned that tractor and tillage parts would not arrive from the United States before spring seeding time.[63] White's truck dealers threatened to resign en masse if the White Western Star plant was not sold to Bow Valley and Nova. A mass resignation would increase off-balance-sheet liabilities by

$30 million in returns of unsold trucks and parts.[64] Dealers also asserted that their business was deteriorating as a result of the uncertainty.[65]

White Canada creditors imposed an effective deadline on the negotiations by filing bankruptcy petitions. Two separate creditor groups petitioned to have White Canada declared bankrupt to prevent US creditors and White Motor US from delaying the sale of the Canadian plants any longer. Time was running out on the Bow Valley-Nova offer, the government-backed bid by the Canadian consortium for the Brantford plant, and the re-opening of the Brantford plant for the 1981 season. The US Bankruptcy Court in Cleveland heard the case on 12-13 March.[66]

The US court accepted the Bow-Nova bid and a joint purchase of the Brantford plant by Linamar and TIC. The Canadian consortium, including Linamar, Shieldings and an employee group, had bowed out of the bidding process. Instead, Shieldings brought together Stratton Georgoulis of TIC and Frank Hasenfratz of Linamar after it became clear that the rivalry of TIC and the Canadian consortium would kill the chances of a sale.[67] The court decision was based on the combined advantages of Linamar and TIC as owners. A strong TIC shareholding provided the new company with US distribution operations while Canadian majority ownership was necessary to justify government involvement.[68]

In return for continuing provision of approximately $15.5 million in loans and guarantees, the new owners agreed to hire more Canadians, purchase Canadian parts and not to transfer existing ownership before March 1983 without the written approval of both governments.[69] David Dodd of the federal Department of Industry stated that Canadian employment was a less important issue to the EDB than was the prospect that the Brantford operations could increase Canadian exports.[70]

The sale of White Canada was completed in the first week of April 1981. One problem still remained; White US claimed that it was not party to the negotiations and it would not approve the full payout of Canadian claims. White Canada creditors had been assured that if the company was re-organized as a going concern there were sufficient funds for full recovery of their claims.[71] As a result, they continued to service White's Canadian operations during the interim receivership to facilitate a smooth re-organization.[72] White US gave Canadian creditors a choice between an immediate payout of 85 cents on the dollar or a delayed payout after bankruptcy of no more than 80 cents on the dollar. Creditors were disappointed, but agreed to accept the 85-cent offer.[73] They received 22 cents in October 1980, 8 cents in February 1981, 45

cents in June 1981 and the final 10 cents on 16 December 1981.[74] The first two dividends were distributed to Canadian creditors in return for extending the time period for filing the re-organization plan. The final claim on White Canada sale proceeds was not paid out until 15 January 1983 when the UAW won a $4.5 million lawsuit under the Ontario Employment Standards Act.[75]

PROBLEMS AT WHITE FARM EQUIPMENT CANADA LTD.

When TIC and Linamar took over White, it was the third largest combine manufacturer in Canada. It had a smaller market share than its rivals, only 17 to 20 per cent of the Canadian market and less than 3 per cent of the US market, but it had lower overhead expenses. It was also the only firm producing axial-flow combines.[76] The previous owners had continued to spend on R&D despite financial problems.[77] This laid the foundation for the new company; the model 9700 represented its best opportunity to increase market share. Future plans included the development of a fuller range and to have three new, smaller axial-flow combines in dealers' showrooms by 1985.[78] The model 9700 took fifteen years and cost $12 million to develop, including a $2.5 million federal grant.[79] It is one of the most costly, sophisticated, and profitable farm machines, with a $112,000 price tag when equipped to harvest wheat. Axial-flow combines separate grain from plant stalks in a rotating drum. They have fewer moving parts and hence require less maintenance than conventional combines. They also work faster and are best suited to huge farms found only in the North American West. White Farm also had an established network of 180 dealers with another fifty dealers under a Quebec distributor. Marketing arrangements with TIC farm operations in the United States allowed it to provide dealers with a full line of farm equipment.[80]

Delays in the springtime negotiations gave White Farm a slow start to the 1981 season. As 1980 had been a bad year for farm equipment, the plant shutdown did not cause a complete elimination of dealer inventory.[81] However, after the resumption of production, new combines did not come off the line until 1 June and sales were lost to competing firms.[82] The farm-equipment season for sales begins in April and peaks in June and July.[83]

White Farm had unexpected setbacks in 1981 which, combined with its short production season, caused financial difficulties. Poor circum-

stances included high interest rates, competitive discounting and sales incentives, such as generous cash rebates and waivers on financing charges, which cut into White's profit margin.

The 1981 summer selling season was unprofitable and in September and October, White Farm laid off 250 production workers and 25 per cent of its salaried staff.[84] Financing was a consistent problem. On 26 March 1982 White Farm was unable to meet its payroll and the plant was closed.[85] The company lacked the level of inventory financing necessary to support its sales volume, but the balance sheet was strong. There was $62.077 million in current assets, $32.834 million in current liabilities, a current ratio of 1.9 and working capital of $29.793 million.[86]

Takeover by TIC investments

White Farm experienced financial difficulties in part because of continuing friction between the two owners and delays in payments for equipment moving between the two companies.[87] On 26 March 1982 the plant was closed when the company ran out of cash. Georgoulis of TIC had refused to either guarantee the necessary financing or to accept Ottawa's conditions for an additional $20 million in loan guarantees.[88]

TIC made an offer of $4.5 million to buy out Linamar. Previous agreements required that both governments give written permission for the transfer of ownership. The takeover bid met with angry reactions from government. It was felt that TIC used 'unhealthy pressures' to force the sale; i.e., it had laid off the Brantford workers to force quick approval. Liberal MPP Robert Nixon told the Ontario legislature that TIC had withheld payroll funds until the final moment to keep the company off balance.[89] There was also a fear that TIC would close the Canadian plant and move the combine production and technology to the United States.[90]

The Ontario government gave its approval on 3 April in the hope that the plant would re-open immediately. The federal government was critical of this decision, since it wanted the company to remain in Canadian hands and felt that creditors could run the firm until a Canadian buyer could be found.[91] The federal government finally approved the sale on 20 April and allowed TIC to keep the $10.5 million in federal loan guarantees in return for the following promises:

– A guaranteed Canadian employment level at 1,200 as long as economic conditions permit.

- Continuation of Canadian 'sourcing'.
- Assurance that the plant will remain in Canada.
- Continuation of farm-machinery manufacturing in Canada.
- Maintenance of R&D efforts.
- Favourable pricing and distribution for Canadian-built combines in the United States.
- Full access for Canadian goods to export markets.
- TIC must relieve the EDB of its $10.5 million in loan guarantees within two years.[92]

More problems under new ownership

On 6 May 1982, immediately after the TIC takeover, the White Farm employment level rose from a skeleton staff to 741 hourly rated and 283 salaried workers.[93] Six weeks later, layoffs began again. It had become apparent that the summer 1982 season would be the third consecutive year of poor farm-equipment sales.[94] It was in July that employee relations deteriorated. White Farm laid off more workers, rolled salaries back to 1979 levels, and reduced employee benefits. Laid-off workers and remaining staff members with reduced compensation packages launched lawsuits against the company.[95]

By the fall of 1982, White Farm was operating on a skeleton staff of about 150 workers and no plans had been announced for the resumption of Canadian production. White president Robert Fuller said that the current inventory level would satisfy demand for at least a year. One hundred employees continued to work on the development of new axial-combine models. The major source of revenue was the distribution of tractors and tillage equipment made by the US parent company.[96]

In addition to federal loan guarantees, White Farm relied on $5.3 million in Ontario Development Corporation (ODC) guaranteed loans and a $2 million concessional ODC loan. In the event of a loan default, the ODC had the right to prevent the company from going into receivership for ninety days. The principal investor was Borg-Warner, with $60 million in financing for inventory in dealers' showrooms.[97]

By January 1983 White Farm was in serious financial trouble. The City of Brantford was threatening to seize assets in lieu of $145,000 in overdue business taxes. Concerned lenders demanded an operating plan by 18 January.[98]

In early March 1983 the ODC was notified that White Farm was in default of its debt agreements. The ninety-day agreement was invoked while TIC, Borg-Warner, the ODC and the federal government tried to come up with a financial re-organization plan.[99] White Farm was actually up to date on all of its loan payments, but was in violation of financial ratios stipulated by the banks.[100]

Borg-Warner reportedly offered an additional $20 million on the condition that the Canadian governments give it first priority on White Farm's assets, including the combine technology, in the event of a loan default. The Ontario government was willing to negotiate, but the federal government was not. It had lost faith in TIC.[101] Nothing was forthcoming in the way of a business plan for bringing back 900 workers after nearly a year of layoff.

Terry Godsall of Shieldings Investments Ltd. stated that 'Borg-Warner was offering another band-aid solution to keep the Canadian operation alive for the short term as a market for White farm products. What is needed is a detailed business strategy for the Canadian company as an active, manufacturing and distributing entity.'[102]

On 9 June 1983 the ODC's ninety-day holding period ended. The defaults by the company, which were now beyond mere technical issues, and the lack of any definitive restructuring proposal prompted White's lenders to call over $15 million in loans. As White failed to make payment, the federal and Ontario governments honoured their guarantees and made payments to the secured lenders.[103]

Receivership

On 9 June 1983, the Royal Bank, Roynat Ltd. and the Mercantile Bank of Canada called $15.5 million in White Farm loans, to be paid by 16 June. White Farm was unable to pay its employees and neither the US parent nor Borg-Warner would put more money into the operation.[104] On 14 June, the Royal Bank appointed Peat Marwick Mitchell of Toronto as interim receiver.[105] A federal government official stated that the assets of White Farm had been valued at $13 million.[106]

In early July, Peat Marwick placed ads in the *Globe and Mail* and the *Wall Street Journal*. They also contacted a number of companies in the industry that might be suitable buyers for the firm. The ad stated that all bids, accompanied by a $0.5 million refundable deposit, were to be submitted by 5 August 1983.[107]

The Borg-Warner Acceptance Corporation of Chicago suggested that it would back any buyer and the dealer organization, but did not originally plan to submit an offer to purchase the company.[108]

A further possible bidding group, composed of White Farm employees, was discouraged from making an offer. A report, 95 per cent funded by the province of Ontario, was prepared by Touche Ross and Partners of Toronto in August 1983. The report recommended against an employee buy-out. It concluded that the firms' difficulties were caused by poor management as well as external circumstances. Forecasts under a scaled-down scenario indicated that the firm was expected to lose money for at least two years and would experience an 'alarming' rise in its debt-to-equity ratio during this period.[109]

The following three bids were examined by the receiver, secured creditors and federal and Ontario government representatives at a meeting held on 30 September 1983.[110] The third bidder, Farm King Ltd., was given until mid-October to complete its offer.[111]

White Farm Equipment US[112]

This bid was rejected; it was considered unacceptable by the receiver and the two governments. The amount of the bid was inadequate, and there were no guarantees that the company would stay in operation or that its axial-flow combine technology would remain in Canada.

Massey Ferguson[113]

Massey Ferguson was rumoured to be offering about $1 million for White's axial-flow combine technology and some of its engineering operations. If this bid were accepted, White's other assets would be liquidated.

Farm King Ltd. (of Modern Manitoba)[114]

This bid totalled $11.6 million and involved keeping the firm operating, but moving the assets and production to Winnipeg. Farm King Ltd. would put up $1 million and its minority partners, 120 Canadian dealers, would put up $.75 million. The Manitoba government was also reported to be supplying $2 million in support of this bid.

In mid-October, the $11.6 million bid from John Buhler, president of Farm King Ltd., was rejected. The remaining prospective purchaser was Massey Ferguson Ltd. of Toronto plus a new bid by the Borg-Warner Acceptance Corporation of Chicago. Robert Terry, the Kansas City divisional manager for Borg-Warner, stated that it was their intention to sell White Farm to 'a Canadian individual we feel can run the business and to give the buyer help with refinancing, working and operating capital'.[115] The identity of the Canadian buyer was not revealed until negotiations had been completed.

On 21 October, the Massey Ferguson bid was rejected and the receiver concentrated on negotiating a going-concern sale with Borg-Warner. Andrew Croll of the ODC stated that Borg-Warner had submitted two previous proposals which had been rejected. The current proposal offered White Farm creditors funds equivalent to the amount that could be expected under the Massey Ferguson bid with liquidation of the company.

The Borg-Warner takeover required Supreme Court of Ontario and FIRA approval. Federal government support was conditional on:

- The successful bidder's attempting to preserve White's Canadian dealer network.
- White's axial-flow combine technology remaining in Canada.
- The availability of parts and supplies for farmers operating White equipment.[116]

The sale to Borg-Warner was scheduled to close on 5 January 1984. It would increase employment at White Farm from the current level of five to 100 employees by the end of January. Facilities were to remain in Brantford.[117]

As of 17 December, the last remaining obstacle was an agreement between Borg-Warner and the UAW. The current White Farm contract was to expire in March 1984 and Borg-Warner insisted, as a condition of sale, that a tentative agreement be reached prior to completion of the transaction. On 15 December, Borg-Warner terminated its purchase agreement and asked for a refund of its deposit when negotiations with the UAW broke down. The two parties disagreed on an 'upfront' 50-cent cut in accrued cost of living adjustments. Bargaining resumed under the encouragement of Brantford mayor David Neumann and Derek Blackburn, the NDP MP for Brantford.[118] The agreement with the UAW

was reached on 18 December and was approved by White Farm workers on 23 December. The new three-year contract tentatively included:

– Continued COLA but the union will waive the first 50 cents to accrue under the new contract.
– The company will not make payments towards supplementary unemployment benefits for the first two years but will begin making payments in the third year.
– Base wages will be frozen at current levels.
– Management and the union will reduce the number of job classifications.
– The company will pay $1.5 million of an estimated $2 million in settlements outstanding to workers. Of this amount $500,000 will be paid when the sale is completed and the remaining $1 million will be held in trust, to be paid when the new contract is ratified.[119]

This tentative agreement between the UAW and White Farm's new owners 'contains expressions of intent about the new agreement, but what will actually happen in negotiations depends on the good faith of the two parties.'[120] When the tentative agreement was ratified by 82 per cent of White Farm workers, the sale agreement with Borg-Warner Acceptance (Canada) Ltd., a subsidiary of the Borg-Warner Corporation of Chicago, was rescheduled to close on 16 January 1984.[121]

SALE OF WHITE FARM EQUIPMENT CANADA LIMITED

On 19 January 1984 it was announced that ownership of White Farm had formally passed to Bill Sinclair of Oakville.[122] Mr. Sinclair is the new president and sole shareholder of the new company, White Farm Manufacturing Limited. He is also president of Caneco Resources Inc. of Oakville, a company with oil and gas interests in the United States. Sinclair initially approached Peat Marwick and Borg-Warner in the summer of 1983 about buying White Farm. In November 1983, Sinclair paid $10.2 million to buy the financing company, White Credit Corporation of Canada of Burlington, Ontario. It was previously owned by the White Motor Corporation of Cleveland.[123]

Borg-Warner lent the new company approximately $7.5 million toward the purchase price, which included a $4.8 million price tag for remaining assets and the assumption of $2.7 million in liabilities. A

further $35 million of funding will be provided 'over a period of time'. In a letter to the receiver, Borg-Warner estimated that $10 million would be needed after the sale closed to prepare for re-opening and that another $10 million would be needed in the first eighteen months of operation. Although Mr. Sinclair is the sole shareholder, Borg-Warner retains effective control of the company in the form of debentures which can be converted into common shares carrying at least 51 per cent of the voting rights.[124] Borg-Warner will exercise the right to convert only if the company goes into default.[125]

On 9 November 1983, when the Supreme Court approved the sale to Borg-Warner, federal and Ontario government guaranteed loans to White Farm totalled $16.7 million. With estimated net proceeds of $7.9 million, a shortfall of $8.8 million was expected, which would cost Canadian taxpayers about $8 million. The Ontario government loans were guaranteed 100 per cent and the federal loans 90 per cent.[126] Government financial involvement with White Farm was expected to end after completion of the Borg-Warner purchase. ITC Minister Lumley said, 'You can believe we won't be putting anymore money into White'; and Croll of the ODC said, 'there will not be any more ad hoc special treatment for White Farm'. On 14 May 1984, Bill Sinclair told reporters that 'White now has no government backing'.[127]

White Farm's troubles have also engendered high costs for, and poor relations with, dealers. A spokesman for the Western Canadian Association of White Farm dealers, Percy Schmeiser, stated that 'dealers have to this point footed the bill . . . It has been very difficult to sell White Farm equipment while the company has been in receivership'. He also claimed that dealers have not received volume bonus awards or warranty claims from Borg-Warner. In addition, Borg-Warner representatives have threatened to sue some dealers for past-due interest and for money held back by dealers in lieu of bonuses and warranty claims.[128]

As the new president of White Farm Manufacturing Limited, Mr. Sinclair faces serious challenges. White needs a heavy emphasis on marketing to promote the advanced technology of its combines and to convince dealers and farmers that 'White equipment and the servicing will be around for years to come'.[129] He announced in January that there will be a gradual recall of workers over the next few months, first for parts production (the most profitable aspect of the operation) and then for combines production. The first machines were scheduled to roll off the line in May 1984.[130]

In early February, Sinclair met with dealers in Brantford and Regina to announce new promotion strategies and interest deals. New White Farm equipment on dealers lots during the company's financial troubles (worth $30 million) will qualify for an interest deferral program and used equipment will be carried at a lower interest-rate. Sinclair said that the company's outlook is good. He noted record turnouts for recent dealer meetings.[131] As of year-end 1984, his favourable projections appear to be materializing; the company is performing well under new management, without government assistance.

On 14 May 1984 the first combine in two years rolled out of the Brantford plant. The first axial-flow combine appeared on 5 July 1984. By that time, White Canada's entire 1984 production had been sold with 50 per cent going to foreign buyers. Sinclair plans to increase exports to 75 per cent of production. He also plans to lengthen the plant's production period by selling machines on advance order.

Sinclair has also developed good relations with employees. The tentative three-year contract with the UAW was ratified on 13 July, paving the way for the distribution of $1 million in deferred holiday payments to current and former White Farm employees two weeks later. Employment at the Brantford plant is expected to remain at 530, rather than returning to its former level of 1,100 workers.[132]

APPENDIX 4A: CHRONOLOGICAL ORDER OF EVENTS

1900
Incorporation of White Motor Co., Cleveland Ohio; truck and bus manufacturer.

1909
White Motor Co. begins selling trucks in Canada.

19 April 1929
Canadian business becomes a separate region dealing directly with head office in Cleveland, in the 'export region' of White Motor Co.

28 May 1931
Opening of new Montreal plant.

.29 September 1945
White breaks ground for new $2.5 million bus and truck plant in Montreal.

2 January 1947
White Canada announces private sale of $1.375 million in first-mortgage bonds.

1948
White Canada widens its sales organization and branch operations.

1950
White Canada agreement with Flexible Co., Ohio to produce, sell and service Flexible buses.

1954
Bus and truck production in Montreal ends for economic reasons.

1956
In response to expected increase in sales, White Canada invests $2 million in expansion. New head office and service centre in Toronto, sales and service centres in major cities.

11 August 1956
White Canada completes move into new west-end Toronto head office.

20 October 1956
White Canada opens $.5 million Toronto branch on Dorchester Ave., Etobicoke.

1960
White US buys Oliver Corp., a Chicago farm-implement firm.

1960s
White US grows rapidly, with numerous corporate acquisitions.

18 November 1961
White US negotiations to buy Cockshutt Farm equipment of Brantford; manufacturer of farm machinery with 750 Canadian and 150 US dealers.

December 1961
White-Freightliner highway-truck production begins in Vancouver. Association with Freightliner of Canada Ltd., Burnaby, BC makes White responsible for sales and service of Freightliner products in Canada.

1 February 1962
White completes takeover of Cockshutt for $31 million. Farm-machinery division to be run as a Canadian subsidiary of the Oliver Corporation.

June 1962
Re-arrangement of Cockshutt manufacturing facilities is completed; production begins.

July 1962
White Motor of Canada begins producing heavy-duty trucks in Brantford, supervised by Cockshutt, in Cockshutt plant addition that was formerly in steel warehouse.

February 1963
First Canadian White truck since 1954 rolls off the assembly line in Brantford.

October 1963
White US merges with Cummins Engine Co.

16 November 1963
Cockshutt Farm Equipment Canada Ltd. chooses Regina site for new wholesale and distribution headquarters; building to cost $.35 million.

13 August 1966
White Canada announces Kelowna BC site chosen for $4 million custom-truck factory because of incentives and Auto Pact; plant to be built in early 1967.

1969
White US acquires Alco engines from Studebaker-Worthington and issues series A preferred stock.

1969
Turning point for White US; 270th largest US corporation with $.75 billion annual sales; 1969 final quarter dividend exceeded earnings.

Early 1970s
White US headquarters move from Cleveland, Ohio to Farmington Hills, Michigan.

13 January 1973
Thanks to Auto Pact, 80 per cent of Kelowna plant output is exported to the United States.

February 1973
White opens Guelph plant for Euclid division, producer of heavy-duty mining trucks.

1975
White US begins omitting dividends on series A preferred stock.

1976
White does not make scheduled redemptions of series A preferred stock due to restrictions imposed by its debt instruments.

1 August 1977
Sale of Euclid Inc. subsidiary to Daimler-Benz AG.

August 26, 1977
White US announces new 364-day revolving-credit agreements with US and Canadian banks for over $300 million. Since June 1976 White reduced its debt by $85.5 million through divestitures.

6 September 1979
White announces exchange of common stock for preferred stock to settle lawsuit brought against it by subsidiaries of Studebaker-Worthington.

31 July 1980
White reports a seven-month loss of $.324 million.

August 1980
Brantford plant closes due to poor sales; 1,100 workers laid off.

4 September 1980
White US files for court protection under US Bankruptcy Act two days after expiration of one-year revolving-credit agreement. White Canada also placed in receivership.

9 September 1980
400 White Western Star assembly plant workers in Kelowna laid off for ten days.

12 September 1980
At White Canada's request, Supreme Court of Ontario appointed Clarkson Co. Ltd. of Toronto as interim receiver. White Canada proposes debt moratorium until 31 January.

September 1980
White Canada losing $2 million per month, mostly from farm-equipment division.

7 October 1980
First meeting of creditors. Date for presentation of re-organization plan changed to 15 December. Creditors elect team of inspectors.

12 November 1980
Unidentified bidder for Brantford plant is said to be preparing report for FIRA. Bidder indicated would buy White's US farm-equipment subsidiary, with or without Canadian operations.

19 November 1980
TIC buys US farm business of White. Presentation of re-organization plan to Canadian creditors postponed until 15 January.

9 December 1980
Bow Valley and Nova Corp announce their joint offer for White Canada subsidiary.

15 January 1981
White negotiating with Bow Valley and Nova Corp for sale of Canadian truck and farm-equipment business; also discussing sale of US and Canadian truck-related assets to Consolidated Freightways and Daimler Benz.

29 January 1981
White given extension till 17 February to present plan of repayment to creditors.

2 February 1981
ITC Minister Herb Gray deciding whether to sell White Canada's truck and farm-equipment assets to a group of Canadian investors and whether to approve their request for a $10 million low-interest loan.

21 February 1981
Majority of White's thirty-seven Canadian dealers threaten to resign en masse if the company does not acccept offer from Bow Valley and Nova Corp.

25 February 1981
Re-organization deadline extended to 31 March if certain conditions are met by 18 March. US Bankruptcy Court to decide between bids by Canadian consortium and TIC.

28 February 1981
White US fires Andrew Zaleski (president of White Farm) and suspends president of Canadian truck division for taking part in a bid.

2 March 1981
US Bankruptcy Court in Cleveland considers various bids for Canadian assets. Effective deadline imposed by Canadian creditors filing bankruptcy petitions.

14 March 1981
US Court approves joint purchase of Canadian farm division by Linamar Machines Ltd. (50.1 per cent) of Guelph and TIC of Dallas. White Farm president re-instated.

16 March 1981
Price of Brantford combine plant announced: $4.5 million in US funds.

17 March 1981
White US announces Bankruptcy Court approved sale of Canadian truck and farm-equipment division assets.

18 March 1981
Ontario court and creditors approve sale of White Motor Canada farm division to Linamar and TIC Truck division sold to Bow Valley and Nova. Last approval still to come from FIRA.

21 March 1981
White Canada asks UAW to take a pay cut.

30 March 1981
FIRA accepts TIC-Linamar proposal for White's farm-equipment division with Ottawa receiving option to buy 14 per cent, Ontario 7 per cent in return for loans and loan guarantees. Buyers agree not to transfer existing ownership before March 1983 without written approval of both governments. Ontario government gets right to delay putting company in receivership for ninety days, should banks call loans.

30 March 1981
Brantford workers ratify new three-year contract.

1 April 1981
Linamar-TIC deal closes.

2 April 1981
Bow Valley-Nova deal closes.

7 April 1981
White Canada's creditors approve 85 cents on the dollar payout.

June 1981
Brantford combines roll off the line.

29 June 1981
Delay in payments from sales of assets causes temporary reduction in payments to creditors.

15 August 1981
Late start, weak Canadian dollar and high interest rates cause weak summer sales for White: 250 of 700 workers recalled since 1 July are laid off and salaried staff reduced 25 per cent to 250.

14 September 1981
Employment down to 400 at Brantford plant; will increase to 700 again in November to produce inventory for 1982 harvest season.

21 March 1982
340 workers recalled after two-week plant closing in Brantford.

26 March 1982
Brantford manufacturing operations suspended: 925 workers laid off due to cash-flow problems.

2 April 1982
TIC offers to buy out Linamar.

3 April 1982
Ontario government approves the offer.

17 April 1982
Federal government approves TIC offer in return for job and technological guarantees. Brantford plant produces axial-flow combines which were developed with the aid of federal grants.

20 April 1982
TIC completes takeover; pays Linamar $4.5 million.

5 June 1982
TIC begins laying off employees.

8 July 1982
White Farm announces layoffs, pay cuts, reduced employee benefits.

17 July 1982
White Farm workers plan legal challenge of pay cuts.

20 October 1982
White Farm layoffs and selective re-instatement of raises; operating Brantford plant on skeleton staff.

5 January 1983
1,100 unemployed White Farm workers win $4.5 million claim under Ontario's Employment Standards Act.

Early March 1983
ODC notified by White Farm's banks of default, invokes ninety-day receivership agreement.

9 June 1983
Ninety-day receivership period ends, Royal Bank, Roynat and Mercantile Bank call $15 million in loans. White Farm not able to meet payroll.

14 June 1983
Peat Marwick Mitchell Co. of Toronto appointed as receiver by the Royal Bank.

15 June 1983
Industry Minister Ed Lumley discloses that several companies are interested in buying White Farm.

13 July 1983
Peat Marwick advertises that all purchase proposals, accompanied by a $0.5 million refundable deposit must be submitted by 5 August 1983.

30 September 1983
Meeting of receiver, secured creditors and government representatives to consider the bids of White Farm Equipment US, Massey Ferguson and Farm King Ltd. White Farm US bid rejected.

Mid-October 1983
Farm King bid rejected.

21 October 1983
Massey Ferguson bid rejected; receiver negotiating a going-concern sale with Borg-Warner. Closing of the sale scheduled for 5 January 1984.

15 December 1983
Borg-Warner terminates its purchase agreement due to unsatisfactory negotiations with the UAW and asks for a refund of its deposit.

18 December 1983
Borg-Warner and the UAW reach agreement on the new contract to be negotiated in March 1984. A new purchase agreement is scheduled to close on 16 January 1984.

23 December 1983
White Farm workers approve the agreement. The Canadian buyer backed by Borg-Warner is announced. Bill Sinclair of Oakville, the new owner of White Credit Corp. of Canada to be the new president and owner of White Farm Manufacturing Limited.

19 January 1984
Announcement that ownership has formally passed to Bill Sinclair.

February 1984
Sinclair presents new promotion strategies and interest-deferral program to dealers.

20 February 1984
Fifty workers are recalled for parts production, 200 more to return in March and the plant to be fully manned with all production lines running by late April.

14 May 1984
First combine rolls off the line at the Brantford plant.

5 July 1984
First axial-flow combine is produced; entire 1984 production has been sold, half to foreign buyers.

13 July 1984
Three year UAW contract is ratified.

26 July 1984
Deferred holiday payments distributed to 800 current and former employees.

APPENDIX 4B[122]

AREAS OF DIFFERENCE IN CANADIAN AND US BANKRUPTCY LEGISLATION

Requirements at time of filing

Canada

Debtor must be insolvent to lodge a re-organization proposal and receive protection from creditors' claims.

US

Debtor can file for a Chapter 11 if he meets or *may* meet the requirements of the Bankruptcy Code as debtor. In practice, a firm which has filed will soon meet the insolvency requirements. Even with a freeze on payables, outstanding purchases are normally changed to COD or CIA (cash in advance), so the firm quickly becomes short of cash.

US re-organization plan vs. Canadian proposal

The two are similar in form and percentage of creditors votes required.

Canada

Only the debtor may file a proposal and it is usually filed to commence proceedings. The first meeting of creditors is normally held within thirty days of filing, at which time a vote is taken on the proposal. Rejection places the debtor in immediate bankruptcy.

US

The debtor under Chapter 11 is given a 120-day stay of proceedings during which time it can continue its business and develop a re-organization plan. This time limit is frequently extended by the US court. After the time expires, any interested party (e.g., a creditor or prospective purchaser) can file a plan for the debtor with the court.

The major difference is that US creditors have to wait months before knowing whether a plan will be forthcoming.

Actions which can terminate a proposal or end Chapter 11 tenure

Canada

The creditor can refuse to approve at a general meeting; there can be a default in the proposal; or there can be a third-party application to annul the proposal because an injustice is being done to allow it to continue.

US

Proposals can be terminated if it is proved, on a third-party motion, that continuing losses are excessive, that there is no prospect for a re-organization plan, that there has been unreasonable delay in effecting a plan, that the court has refused to accept the plan or that the debtor has defaulted.

Administration of a re-organization

Canada

Re-organization proposal is lodged with a licensed trustee, who will review the debtor's circumstances and prepare an independent report to the creditors on the feasibility of the proposal. Often the services of an interim receiver are used to monitor the operation for the creditors, assist the debtor to obtain trade credit, review transactions outside the ordinary scope of business and take control of cash receipts and disbursements.

US

Re-organization may be conducted by a 'debtor in possession'; that is, the debtor becomes its own 'trustee' responsible for developing a re-organization plan, administering claims against the estate and conducting the business of the firm. The court will only impose a trustee where it can be proven that the debtor has committed fraud or that existing management is guilty of gross mismanagement. The court can appoint an examiner to review the debtors plan and other matters.

The difference in the White Case is that Canadian truck operations were able to conduct regular business while US truck operations were not.

Creditors' representatives

Canada

Canadian creditors perceive they exercise some control over the debtor and trustee through the involvement of their elected representatives: up to five inspectors who function like a board of directors and can monitor and influence their eventual recovery

US

The court appoints a creditor committee – a group of observers able to exert only modest influence on the court.

Negotiations

Canada

Sale negotiations are conducted by management in concert with an interim receiver. Transactions may require court approval and approval at a creditors' meeting

US

Chapter 11 provides for continued debtor administration of assets, subject to court approval.

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5
Cooperative Implements Ltd.

BACKGROUND

Cooperative Implements Ltd. was organized in 1948 in Winnipeg, Manitoba to manufacture agricultural implements. The company, whose main plant is in Transcona, Manitoba is the only farmer-owned agricultural implement manufacturer in Canada, and the largest in North America. As of 31 October 1983 when the minimum membership investment was raised to $100, Coop Implements' membership fell from the 1982 level of approximately 90,900 farmer Coop members to approximately 25,000.

Before the seven-and-a-half acre Transcona plant was built in the early 1970s, Coop Implements was a marketer of lines (products built in whole or in part by other makers for Coop or adapted to carry the Coop label). Once the large plant was built, Coop's emphasis turned to operational efficiency and marketing strategy in the production of its own machinery. In a traditionally volatile business Coop Implements functioned well until 1977 when it felt the full impact of the downturn in the farm-machinery business cycle. In 1977 Coop lost $9.1 million on sales of $65.5 million. Higher fuel prices, low commodity prices, high interest rates, and higher input costs for items such as fertilizer forced farmers to postpone the purchase of machinery. Coop was caught with a large inventory when sales were slow. The company also faced an acute capital shortage, and could not repay $30 million in overdue loans owing to banks, cooperatives and credit unions.[1] By mid-1977 employment had

fallen from a 1976 high of 800 across the Prairie provinces to a small maintenance staff at the Transcona plant.[2]

In January 1977 Coop Implements approached the Manitoba government (then NDP) with a request for financial equity assistance. In April 1978 the new Conservative government of Manitoba, in co-operation with Saskatchewan and Alberta, agreed to provide $7 million in loan guarantees for Coop. The federal Department of Agriculture provided $8 million in a recoverable contribution, and the wheat pools, co-operatives, and credit unions which backed Coop Implements agreed to provide additional resources. This financial package effectively saved the company from receivership.

Coop Implements recovered but, in April 1980, made a second request for assistance. The purpose of the new financial package was not to save the company from bankruptcy, but to aid in improving its equity position through the conversion of debt to equity. The company also wanted to expand its facilities to meet the potential growth in demand which was forecast as farmers became unable to put off capital purchases any longer.

In February 1982 a $45 million refinancing package consisting of share purchases by the co-op groups and loans from the federal and Prairie governments was announced for the re-organization of Coop Implements. In addition, members were required to raise equity of $5 million over five years.

Cooperative Implements has retained its market share. However, sales fell in the first six months of 1983 to $82.4 million, down 12 per cent from 1981 levels over the same period. Competition is stiff in a difficult market, and profit margins are declining as manufacturers offer discounts and special financing to encourage sales. The company intends to continue the cost-cutting and retrenchment begun in 1982 – reducing assets and inventories, laying off excess staff, restricting research and development (an area it entered vigorously in 1980-81), and abandoning aggressive growth in favour of the 'bottom line',[3] that is the re-establishment of a profitable position.

1977-80: COOP IMPLEMENTS' FIRST REFINANCING PACKAGE

Cooperative Implements Ltd. is a major western producer-distributor of equipment such as tractors, balers, and mowers, sharing this position with another Winnipeg firm, Versatile Manufacturing Company. Both

companies had few major financial problems until 1977. The year 1975 was a profitable one ($2 million), and in 1976 Coop showed a profit of $1.6 million. In the same year sales climbed 22 per cent to $92 million. On 31 October 1976 (the end of the agricultural industry's fiscal year), Coop Implements had current liabilities of $34 million, long-term debt of $6 million and total assets of $57 million. Banks, co-operatives and credit unions were relied upon for loans. At this point Coop Implements had 1,364 employees across the Prairies, with 800 at the plant in Transcona.[4] Thus, Coop's direct economic impact in terms of employment was concentrated in Manitoba where Lloyd Axworthy, a Liberal cabinet minister during the assistance period, was a Winnipeg MP. Coop Implements had sixty-eight retail depots through the Prairies,[5] and thousands of farmers depended on the company for service and parts since it specialized in agricultural equipment particularly suited to prairie farming.

By January 1977 Coop Implements was affected by the depression in the agricultural economy and approached the Prairie and federal governments for assistance. Coop requested $15 million of a $50 million refinancing package from the Prairie governments ($6 million from Manitoba), with the balance to come from the private sector. Higher input costs, low world grain prices, and the spectre of returning drought has made farmers reluctant to purchase capital goods. Coop was caught with a high inventory and a severe capital shortage. Its debt with the Mercantile Bank was $10 million and it owed $32 million in short–term loans to a number of co-operatives, the major lender being Manitoba Pool Elevators.[6] The co-op group extended Coop Implements' loan due date from 31 October 1977 to 1 April 1978 to ensure that Coop would not be forced to default during its negotiations for financial assistance with the Prairie and federal governments.

The political debate

Sixteen months passed between Coop's January 1977 request for aid and the approval of the refinancing package in April 1978. The NDP government of Manitoba had stalled on support for Coop, and a policy had not been decided upon when an election was called in mid-1977 and a new Conservative government gained power. One of the Conservatives' election promises was that failing businesses would not be rescued with public funds. Finance Minister Don Craik stated, concerning Coop Implements, that Manitoba 'cannot at this time commit public funds to that

extent [the requested $6 million].'[7] He claimed that the former NDP government had rejected Coop's request. However, the NDP denied this. NDP members of the Manitoba Legislature, particularly former Co-operatives Minister René Toupin, indicated that Coop had sold $92 million worth of machinery in 1976, employed between 700 and 800 people, and was a major provincial exporter. In addition, Manitoba was to assume only a small part of the risk of the total financing package. The Conservatives countered by noting that Coop had turned down aid from the Manitoba Development Corporation because the MDC would have had first call on assets.[8]

In December 1977 Premier Sterling Lyon stated that the 'door had not closed' on Coop, and that his government might consider loan guarantees, but not equity.[9] Coop Implements had requested equity since its poor sales and large inventories were making it impossible to reduce its debt load or to continue regular production. In October 1977 the Transcona plant had been almost shut down, continuing to operate with only a maintenance staff of production workers. A large number of farmers were dependent on Coop for the parts and servicing of their Coop machinery. Donald Larson, then president of Coop Implements, hoped to raise the employment level to 200 or 300 over the winter to produce spring planting equipment.[10] However, an injection of equity was vital to this plan.

Attempts to raise equity had been made through a share sale. However, the 1977 owner-equity drive had raised only $1 million.[11] The company's severe capital shortage could not be alleviated through banking channels since Coop had exhausted its line of credit. The credit union societies which were Coop's major lenders needed assistance to roll-over the company's debt, which was due 1 April 1978.[12] At this point Coop's uncertain financial position was proving detrimental. Customers were less willing to invest in company equity or to buy machinery. Should Coop fail, the equipment that farmers owned would depreciate.

The government of Saskatchewan was the first to announce its support for Coop Implements. In February 1978, the deputy minister of finance, Murray Wallace, announced that Coop's problems were short-term, and that, therefore, assistance to the company would not be a risk. The government reasoned that Coop Implements had sold $300 million worth of equipment in Saskatchewan, the company's depots employed 300 in the province, and half of Coop's active members were residents of Saskatchewan.[13] Saskatchewan would thus benefit from Coop's con-

tinued operation. The one qualifier regarding Saskatchewan's assistance was that Manitoba and Alberta participate. Wallace believed that support from Manitoba would be the catalyst for support from all interested parties. However, Manitoba continued to be reluctant because the government was not convinced that Coop was viable and found the risk excessive.

Manitoba was also being pressured by the federal government. Eugene Whelan, then minister of agriculture, stated in March 1978 that the Supplementary Estimates provided $8.5 million for Coop Implements.[14] However, Whelan was having difficulty persuading the provinces to match that commitment.

A $23.7-million refinancing package for Coop Implements was announced on 10 April 1978. Co-op groups including credit unions, wheat pools, and Federated Cooperative Ltd. agreed to a loan of $8.7 million. The federal government, through the Department of Agriculture, provided an interest-free loan of $8 million, of which $500,000 was subsequently paid off.[15] Saskatchewan and Alberta contributed $2,625,000 and $1,575,000 in loan guarantees, respectively. Manitoba agreed to provide a $2.8 million loan guarantee with the proviso that the government would have the right to withdraw from this commitment after two years. Finance Minister Donald Craik noted that approximately 2,000 jobs in secondary and tertiary industries would have been affected if Coop had entered receivership. NDP House Leader Sidney Green stated that the bailout was welcome, but it contradicted the Conservatives' election promises.[16] Earlier in the negotiations, the NDP had fully supported assistance to Coop, and had urged the Conservative government to act.

Coop Implements welcomed the assistance. However, conservative production schedules would be maintained because the industry was depressed.[17] All agricultural implement companies, such as Massey Ferguson and White Farm, had large inventories and were experiencing layoffs. Low world grain prices decreased farmers' incomes, and the low value of the Canadian dollar made imported machinery components expensive.

In mid-November of 1978 Coop Implements replaced its top management. David Tait was appointed CEO to replace Don McNeil. He had just restored MLE Industries Ltd., a Calgary-based manufacturer of road-marking materials to profitability. Tait intended to place emphasis on Coop's sales and product-development departments, cut the number of

dealer-service depots to fifty-three, and abandon export efforts while the company regrouped.[18] Coop Implements' financial structure was monitored by a committee with members from co-operatives and the federal and Prairie governments. The committee's chairman is Norm Bromberger, CEO of Credit Union Central of Saskatchewan. Bromberger led the approach to the federal government for further financial assistance in February 1981.

1980-1983: THE SECOND FINANCIAL PACKAGE

In 1979, the first full year of Coop Implements' re-organized operations, the company earned a profit of $1.58 million on sales of $70.7 million. In 1978 Coop had lost $3.8 million.[19] By 1980 gross sales reached $80.5 million. However, the company lost $970,000 due to high interest rates.[20] Interest payments were $4.6 million.[21] Coop's management believed that with a restructuring of short-term debt to long-term, and increased equity support, the company could show a profit.

In February 1981 Coop Implements stated that it was seeking a $30 to $35 million loan and equity plan to enable it to repay its short-term debts, and to put the two-year-old re-organization plan into larger-scale production and marketing. Norm Bromberger, chairman of Coop's administration committee, stated that the $17 million received in 1978 was a temporary lifeline for basic survival. The first package was not 'sufficient equity for the long term. It was [used to enable the company to] survive, and to show that a wholly-upgraded system could be a viable operation.'[22] The long-term outlook was for increased demand for the farm production of western Canada – Coop's market area. The company therefore planned to expand its facilities to meet the potential growth in demand.

The political debate

The reaction from the federal and Prairie governments was that the new proposal would be studied.[23] When pressed in the House of Commons to further assist Coop, the minister of agriculture, Eugene Whelan, stated that Stan Hovdebo, (NDP Prince Albert) 'should realize that [Coop Implements] would have been closed over three years ago if it had not been for the action of the federal government in providing an interest-free loan for $8 million when the other people were not doing very much about it . . . we had to beg the provinces to come into it.'[24] Hovdebo

indicated that Coop needed a fresh $14 million, not the $8 million granted in 1978. The first package had been beneficial, but was now inadequate. Whelan countered that the $8 million had been an interest-free loan, and should therefore be valued at $10 million. This arrangement was far superior to the loan guarantees which Massey Ferguson and Chrysler had received – companies which Hovdebo was using to illustrate government discrimination against a western company.

The matter of federal discrimination resurfaced in December 1981 when during negotiations on a financial package for Coop, the Prairie provinces accused the federal government of unfair treatment and a pro-eastern bias.[25] The provinces threatened to cancel any deal and boycotted a meeting called by the federal officials. The federal Department of Agriculture had offered to provide $7 million in new loans, and to forgo the $7.56 million owed from 1978 to a total of over $14 million. The provinces were insisting on a fresh $14 million, taking the position that 1978 was history. Donald Cody, the Saskatchewan minister of co-operatives, stated that the 'federal offer is more clever accounting than needed assistance.'[26] The federal government had helped Chrysler, Massey Ferguson, and White Farm Equipment with $250 million in loan guarantees, whereas Coop required only $14 million. Whelan persisted with his point that his department had already rescued Coop, and it was the provinces' role to provide a substantial part of any new assistance.

The Manitoba government took the position that it would have to review Coop's operations to evaluate the company's viability. Since Manitoba could have had a representative on Coop's board of directors, but preferred to use an official in a liaison role, the government did not have precise knowledge of the day-to-day workings of the company. Adding to delays in the negotiation process was debate within the Manitoba legislature. Sam Uskiw, NDP agriculture critic, voiced the opinion of his party by questioning whether assistance would 'involve greater opportunities [employment] or are we simply trying to bail out the company again?'[27]

Coop Implements was frustrated by the delays in securing funds to improve its equity position. By mid-1981 the company was operating almost completely on borrowed funds, and interest payments were preventing the attainment of profitability despite strong sales.[28] Coop performed strongly in 1981 while awaiting a settlement of the negotiations for financial assistance. Gross sales increased 30 per cent over 1980 to $105 million, while sales in the overall farm industry grew 28 per cent.

The company followed a policy of aggressive new product development with a line of eleven new farm machines and two improved models. In 1981 $1.5 million (1.5 per cent of sales) was spent on research and development compared to $996,000 in 1980.[29] Only $285,000 had been allocated to product development in 1978.[30] However, Coop's interest bill affected the viability of the company. Although sales were ordinarily high enough to make a profit, the company lost $1.03 million on net sales of $93.2 million[31] because it was faced with an interest charge of $8.4 million.[32] This was almost double the 1980 figure of $4.6 million, and was a cost which could have been avoided had the equity package been in place. Without the increase in interest charges, Coop would have made a profit of $2.8 million. Using this argument, Art Cedergren, chairman of the board, reasoned that 'in a difficult economic environment, the company has gone from a near collapse in 1977 to a position of strength and operational consistency in 1981.'[33]

On 10 February 1982 the federal and Prairie governments and the co-op group ended negotiations and approved a second funding package to a total of $45 million for Coop Implements. An additional $9.5 million was provided from the co-op group through the purchase of preferred shares.[34] The co-op group also agreed to forgive its 10 per cent cumulative dividend, as of 31 March 1982, on its class C shares. The federal Department of Agriculture agreed to provide a total of $21.5 million, or 45 per cent of the package.[35] $8.44 million would be in the form of a loan to be interest-free until Coop had fully recovered its $12.5 million accumulated loss at fiscal year-end 1980.[36] At this point the interest rate charged would be the going rate for farm credit corporation loans. The Department of Agriculture also provided $5.5 million in loan guarantees and a $7.8 million forgiveness on the 1978 loan. The Prairie governments contributed $7 million in a loan which would be interest-free until Coop recovered (Manitoba contributed $2.9 million, Saskatchewan $2.4 million, and Alberta $1.5 million). An additional $5 million was to be raised within five years in owner-equity. The net impact of the package was that it would lower the cost of capital for Coop Implements, and permit the company to use the earnings once directed to interest payments to finance growth.

Following the receipt of the new funds Coop has had a mixed record. In May 1982 the company's normal three-week summer shutdown (a characteristic of the industry) was extended to five weeks.[37] Despite the forecasts of a return to 1976 employment levels, 400 workers were off the

job during this shutdown period. However, while tractor, baler, and mower sales declined nationally from 1980 to 1982, Coop's sales increased by 48 per cent over this period.[38] In 1982 a major contract was negotiated for the export of Coop Implements' diskers to the Sudan. Strong grain sales to China, the Soviet Union, and Brazil by the Canadian Wheat Board have the potential of boosting farm machinery sales. However, as producers face stiffer competition the need to discount is hurting cash flow and cutting profit margins. Coop Implements has taken an aggressive sales approach using techniques such as sales visits to farmers in an attempt to retain its market share. The Prairie Farm Implements Manufacturers Association has indicated that no upturn is forecast in the market and therefore it is likely that Coop will continue its pattern of cost-cutting, retrenchment and conservative production schedules.[39]

NOTES

1 *Canadian Business* June 1979.
2 *Winnipeg Free Press* 30 November 1972.
3 *Credit Union Way* July 1983.
4 *Financial Post* 5 October 1977.
5 *Winnipeg Free Press* 20 October 1978.
6 Ibid., 30 November 1977.
7 Ibid.
8 Ibid., 6 December 1977.
9 Ibid., 21 December 1977.
10 Ibid., 30 November 1977.
11 Ibid., 21 December 1977.
12 Ibid., 3 February 1978.
13 Ibid.
14 *Hansard* 16 March 1978.
15 *Credit Union Way* 17 March 1982.
16 *Winnipeg Free Press* 13 April 1978.
17 Ibid., 15 April 1978.
18 Ibid., 20 October 1978.
19 Ibid., 11 February 1981.
20 Ibid., 11 February 1982.
21 *Credit Union Way* 17 March 1982.
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23 Ibid.; *Winnipeg Free Press* 12 February 1981.
24 *Hansard* 20 November 1981.
25 *Globe and Mail* 17 December 1981.
26 Ibid.
27 *Winnipeg Free Press* 12 February 1981
28 Ibid., 23 July 1981. Sales rose over 40 per cent in 1980.
29 *Credit Union Way* 17 March 1982.
30 *Hansard* 7 December 1981.
31 *Winnipeg Free Press* 15 June 1982.
32 *Credit Union Way* 17March 1982.
33 Ibid.
34 Ibid.
35 *Winnipeg Free Press* 10 February 1982.
36 *Credit Union Way* 17 March 1982.
37 *Globe and Mail* 29 May 1982.
38 *News Service* 31 March 1982 (of the Canadian Cooperative Credit Society).
39 *Credit Union Way* July 1983.

6
Minaki Lodge Resort Ltd.

BACKGROUND

In 1907 the National Transcontinental Railway built a bridge across the Winnipeg River at a site fifty kilometres northwest of Kenora, Ontario. Several years later Minaki Inn was built by the NTR near the crossing. Canadian National Railways absorbed the NTR in 1919, and in 1923 it took over Minaki Inn. The CNR decided to use the inn as a showpiece – one of three stops, including Pictou Lodge in Nova Scotia and Jasper Lodge in Alberta, to show prospective corporate clients on a cross-Canada rail journey. Money was poured in to turn Minaki into a first-class resort. On June 11, 1925, one day before the lodge was due to open, it was completely devastated by fire. Undeterred, the CNR had it ready to re-open in 1927 after thirty trainloads of dirt were shipped in for a new golf course. The lodge soon acquired a reputation as 'one of the most sumptuous resorts in Canada'.[1]

Minaki Lodge fared poorly in the Depression period. In 1933 it grossed only $884.77.[2] The lodge thrived in the 1940s, only to face difficulties in the 1950s as the popularity of rail service declined. In 1955 the CNR sold Minaki and three other lodges to A-T Hotels of Winnipeg, Manitoba. A-T did not wish to purchase Minaki since it was not a profitable proposition. However, it was an 'all or nothing' deal.[3] A-T agreed to sign a contract to operate Minaki for ten years, then immediately sold Minaki to Rod Carey, a private entrepreneur.

The tourist industry in Northern Ontario was severely hurt in the early 1970s by mercury pollution in the English-Wabigoon-Winnipeg river system. Minaki's private operators were unable to operate the

lodge profitably, and were in danger of defaulting on loans to a US industrialist and to the Northern Ontario Development Corporation. In 1974 the Ontario government purchased the lodge for $1.3 million and promptly closed it down. Following extensive renovations the lodge was re-opened on 29 April 1983. It is to be operated for the Ontario government as a first-class wilderness resort by Radisson Hotels Corporation of Minneapolis.

1974-1976: PURCHASE AND RENOVATION

In October 1974 Claude Bennett, then Ontario minister of industry and tourism, indicated that the provincial cabinet had approved a maximum $5 million expenditure for the development of Minaki.[4] Ontario had decided that rather than foreclose on a $500,000 Northern Ontario Development Corporation (NODC) loan to Minaki's private operators, and allow Minaki to default on a loan to an American investor, the government would step in. The government decided to make the purchase so as not to lose the economic impetus that would be gained from further development of the lodge. Minaki Lodge was to act as a stimulus to the tourist industry in northwestern Ontario and thus aid a depressed region. In 1974 the lodge was closed to permit renovation, although the ski hill and the golf course remained operational. Work was financed through Ontario Development Corporation loans and advances to Minaki Lodge Corporation. A joint Ontario-federal government study of Minaki's marketability and viability was undertaken at the time of purchase. Its findings have never been publicly released.

Ontario appointed a board of directors of Minaki Lodge Resort Ltd. whose membership included Industry and Tourism's Frederick Boyer as secretary, and J.E.J. Falgren as chairman. The other members were: David Caswell, Rolland Doucet, W.F.B. O'Brien, Ben Ratuski, and A.T. Spence. William Charlton replaced Ed Falgren as chairman of the board in 1980. The board of directors as of December 1983 consisted of Frederick Bayer (president and CEO); William Charlton, Ministry of Government Services (chairman); Donald Cameron (Ministry of Northern Affairs); A.D. Croll, Ontario Development Corporation; and M.J. Shoreman, Ministry of Tourism and Recreation.

The political debate

The purchase and development of Minaki Lodge was strongly challenged by both opposition parties. Minaki was immediately labelled a 'white elephant' by Robert Nixon, leader of the Opposition.[5] Criticism centered on a concern over northwestern Ontario's dependence on resource industries such as tourism. During the 1976 throne speech debate, Iain Angus (NDP) termed Minaki a frivolous expenditure, stating that a better way to develop the tourist and secondary industries could be found, such as improved health and transportation (surface or air ambulances) in the north.[6]

Opposition MPs repeatedly claimed that the funds being diverted for the development of Minaki Lodge were misplaced. NDP critics noted that Minaki, with a population of 300, had no school facilities above Grade 3. Children in higher grades had to be bused to Kenora, a two-hour journey. The needs of these children should be met before those of the elite to whom the lodge would cater.[7] Bennett, retorted that the lodge was not for the elite, but for the benefit of the tourist industry.[8]

Development of the lodge was to be undertaken at a time of government restraint. The 1976 hospital closures were a hot political issue and provided fuel for the Minaki debate. Boyer, CEO of Minaki Lodge Resort Ltd., questioned 'how in the name of God can we announce another $2 million expenditure when hospitals are being shut?'[9]

By early 1976 Bennett announced that the Ontario government wished to return the lodge to private hands.[10] The second phase of the lodge's development was to be postponed due to 'budget constraints'. Minaki had become a political embarrassment. $1.5 million plus $400,000 in operating costs were left in the estimates for Minaki Lodge.[11] The $400,000 would be used for maintenance, security, the operation of the golf course, the ski hill, and Holst Point – a fishing and hunting lodge. A number of contracts were cancelled and $40,000 of ordered kitchen equipment was returned to the supplier. Minaki was nonoperational because no rooms had been built in the first phase of renovation. At this point Woody Linton, president of the Minaki Community Association stated that Minaki now lay 'between the devil and the deep blue sea.'[12] The lodge's future was an unkown.

In mid-1977 a study of the Ontario Standing Committee of the Public Accounts recommended that Ontario divest itself of Minaki Lodge. However, Bennett and his successor Larry Grossman decided that the government could not pull out now and would instead investigate private-sector proposals including the idea of a public-private partnership in the lodge's operation.[13] One of the factors which contributed to this decision was their belief that Minaki would provide employment opportunities and have spinoff effects in Northern Ontario.

Debate in the community

Bennett predicted Minaki's development would create 250 direct jobs in Minaki (population: 300), and a spinoff of 250 jobs in resource industries in the immediate area.[14] Most of those employed would be native people in an area with one of the continent's highest concentrations of native people. Since Minaki's unemployment rate ran as high as 60 per cent in the winter the prospect of the lodge was attractive.[15] However, by mid-1980 Barry Gibson, an unofficial community spokesman, stated, 'people are skeptical. It's taken so bloody long to get to this point and we still don't see any construction jobs.'[16] The skepticism appears to have been warranted. In April 1983 press reports indicated that when Minaki opened it employed white, middle-class university students. A majority of positions were held by outsiders from Toronto and Winnipeg. Only twenty-five of the 125 employees lived near enough not to have to live in,[17] and of these only fifteen were residents of Minaki.[18] There were eight native people on staff.[19] However, Barry Gibson became optimistic, as is apparent in his announcement at Minaki's official opening on 15 July 1983 that 'every single person in this community who wants a job can get it.'[20]

Community reactions to the development of Minaki Lodge were mixed. Rob Bennett, former president of the Minaki Community Association, stated, 'It's the best thing that could happen to us – it will bring in swarms more visitors.' Another Minaki resident claimed, 'The hotel is run by the Americans for the Americans and the people of Minaki ain't going to see much of the money.' However, Frederick Boyer has stated that every dollar spent on Minaki Lodge generates $3 in the local economy.[21]

The political debate

Ontario cabinet ministers continued to defend the development of Minaki through the late 1970s. In early 1978, Larry Grossman, then minister of industry and tourism, announced that the government had decided to continue the redevelopment of the lodge rather than shut it down and lose its entire investment.[22] On 28 June 1978 Grossman announced the appointment of a task force to negotiate with a hotel/resort chain to operate the lodge for the government upon its completion. Members of the task force included Robert Rubinoff, former executive vice-president of Commonwealth Holiday Inns, David B. Caswell, president of Sheraton-Caswell Inns, Frederick Boyer, and John Maxwell, assistant deputy minister of tourism. In November 1979, Grossman stated that he was 'not convinced that [Minaki Lodge] can't work,' and that he would decide by 31 March 1980 whether to scrap the project, sign a management agreement or sell.[23]

Throughout this period the Opposition pressed the government for a decision. Critics claimed that funds should not be poured into Minaki without the assurance that it would earn a return. Even when closed the lodge was costing $1,000 a day to maintain. The government responded by attempting to turn Minaki's development into a regional issue. Leo Bernier, then minister of northern affairs, stated, 'I don't apologize for this investment in northern Ontario at all. Southern Ontario has had endless capital poured in by government.'[24]

Opposition members refused the bait, and persistently stated that something must be done to boost the economy of northern Ontario. However, spending millions of dollars on Minaki was not the most cost-effective solution. T.P. Reid, then NDP critic of northern affairs, strongly opposed the development of Minaki Lodge. Stuart Smith, then Liberal leader, termed it, 'one of the most foolish expenditures in history.'[25]

On 21 April 1980 Grossman announced that the Ontario government had signed a management contract with Radisson Hotels Corporation of Minneapolis.[26] Since no private interest would buy Minaki, the choice was to scrap the redevelopment and lose $10 million or continue the development with a private manager. Eighteen international and seventeen Canadian hotel chains submitted bids. Radisson was chosen due to its unique experience in operating wilderness hotels, and its low fee of $100,000 per annum. Radisson would oversee construction and develop marketing plans for Minaki. Minaki Lodge would be targeted

for the midwestern US market with the expectation that Minneapolis and Chicago would be the main sources of business. The lodge would also aim to attract the Winnipeg market.

Radisson signed for a fifteen year management term, which can be terminated by the government for any reason with ninety days notice and the payment of a $100,000 termination fee. Radisson will receive $100,000 per year or 5 per cent of gross profit, whichever is more, plus 10 per cent of net profits once Minaki becomes profitable. A $75,000 fee for technical services was included in the contract. All services, equipment, and supplies are to be Canadian whenever possible. Employees are hired by Radisson as agent of the Government of Ontario.

The province does not expect ever to recover its capital investment of $20,969,176,[27] (noncapital investment totals approximately $12 million). Once this investment is written off, Minaki should break even by 1984. An annual profit of $200,000 is then expected from business meetings and conventions, which are the targeted market. Grossman has stated that Minaki Lodge must not be measured in terms of its profits but in terms of the social benefits it will bring to Minaki and northwestern Ontario. Frederick Boyer feels Ontario's aim is 'to establish a tourism flagship in the northwest and put the region on the map.'[28]

1980-83: THE COMPLETION OF MINAKI LODGE

Minaki Lodge opened for guests on 29 April 1983, and officially on 15 July 1983. The occupancy rate for the 1983 season was 60 per cent, just below the break-even level. One press report termed the Lodge a 'wilderness adventure in a setting of big city elegance and sophistication.'[29] This is the atmosphere for which the Ontario government aimed in its bid to establish a world-class hotel and convention centre to attract prosperous families and corporate clients.[30] NDP northern affairs critic Jack Stokes called the lodge 'second to none,' although the funds spent on its development 'could have been used in a more innovative way.'[31]

Public expenditures on Minaki have totalled $45 million. This figure includes $16 million spent on construction, $150,000 on the railway station, $400,000 on community improvements, and $12 million in debts and administration costs.[32] Revenues are not expected to cover these expenditures. Opposition members remain skeptical that the Minaki investment will ever make a return even should its 200-day operating

season (29 April to early November) be extended to year-round in a bid for profitability. Reuben Baetz, minister of culture and recreation, has attempted to divert criticism by claiming that a narrow cost-benefit analysis does not capture the essence of Minaki Lodge. 'Minaki will have a positive historic value, it is the finest small resort in Canada, and has turned Minaki from a ghost town to a world-class resort.'[33]

NOTES

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2 Ibid.
3 Ibid.
4 *Debates of the Ontario Legislature* 29 March 1976.
5 Ibid., 12 May 1975.
6 Ibid., 29 March 1976.
7 Ibid.
8 Ibid., 30 April 1976.
9 *Toronto Star* 30 March 1976.
10 *Debates of the Ontario Legislature* 31 March 1976.
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12 *Toronto Star* 30 March 1976.
13 *Minutes of the Ontario Natural Resources Development Committee* 31 October and 29 November 1977.
14 *Debates of the Ontario Legislature* 25 October 1977.
15 *Toronto Star* 11 June 1983.
16 *Maclean's* 8 September 1980.
17 *Globe and Mail* 30 April 1983.
18 *Toronto Star* 16 July 1983.
19 *Globe and Mail* 30 April 1983.
20 *Toronto Star* 16 July 1983.
21 *Globe and Mail* 1 August 1981; 30 April 1983.
22 *Debates of the Ontario Legislature* 21 April 1980.
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26 *Debates of the Ontario Legislature* 21 April 1980.
27 Ibid., 17 December 1982.
28 *Globe and Mail* 1 August 1981.

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32 Ibid.
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7
Clarke Irwin Company Limited

BACKGROUND

Clarke Irwin Company Limited in Toronto was one of the first publishing companies to benefit from the Ontario Government Book Publishing Development Program. This program provides qualifying publishing houses with loan guarantees and interest subsidies.

General industry problems, adverse economic conditions and firm-specific difficulties combined to cause financial problems for Clarke Irwin. Operations for the fiscal year ending 31 January 1983 resulted in a 30 per cent drop in revenue.[1]

The exact reason for the withdrawal of government support in May 1983 is difficult to pinpoint. The outgoing president, William Clarke Jr., described the firm's past performance and future prospects much differently than did Ontario government representatives.

The company

Clarke Irwin was founded in 1930 by William Clarke Sr. and his brother-in-law John C.W. Irwin. In 1944, following a disagreement with his brother-in-law, Mr. Irwin left the firm and in the following year founded the Book Society. When William Clarke Sr. died in 1955, his wife moved up from vice-president to president and ran the firm for ten years. In 1965 her youngest son, William Jr., formally joined the firm; he became vice-president in 1967 and president in 1981. William Clarke Jr., who had completed a doctorate in astrophysics at UCLA and has a strong interest in computers, had not planned to work in the family firm other than on a part-time basis.[2]

For the first three decades of business, Clarke Irwin was a major educational publisher. Its textbooks were a major presence in classrooms between 1930 and 1965.[3] In the 1930s and 1940s some general books were added to the list, but textbooks were the predominant strength of the firm until the late 1960s. In the early 1970s there was a change in emphasis to publishing trade books. Textbooks had represented 75 per cent of the business until the late 60s; in the late 1970s they made up only 25 per cent of Clarke Irwin's book list.[4] William Clarke Jr. presided over the company's transformation from a textbook house to a general publisher. In the early 1980s, Clarke Irwin was one of the five largest and most distinguished Canadian-owned publishers in Canada.[5]

Ontario government support for the publishing industry

The Ontario government founded the Book Publishing Development Program in 1972. The loan-guarantee program, prompted by the failure of the Ryerson Press, was put in place before the report of the Ontario Royal Commission on Book Publishing in 1973. The program is run jointly by the Ministry of Citizenship and Culture and the Ontario Development Corporation (ODC). Its objectives are to improve access to bank loans by publishers and to address the undercapitalization of the publishing industry.[6]

To qualify for the Book Publishing Development Program, a publisher must be 75 per cent Canadian-owned and have annual net sales of Canadian-authored books between \$150,000 and \$625,000.[7] Aid is provided in the form of either loan guarantees to a combined maximum of \$250,000 or interest-rate subsidies equal to 50 per cent of interest payments based on the prime rate up to a maximum of \$50,000 per annum. When the \$250,000 loan-guarantee limit was introduced by the ODC in 1978, McClelland and Stewart and Clarke Irwin had already been granted guarantees in excess of this value.[8]

Of the twenty-three independent Canadian publishers in the development program, fourteen had loan gurantees at the start of 1983. Further, the ODC had \$5 to \$6 million outstanding in loan guarantees and interest subsidies to qualified publishers.[9]

If not for federal and provincial support, much indigenous Canadian publishing would not take place. It is extremely difficult for general publishers to survive without aid. The Ontario government is very generous in terms of its support to writers and publishers. Ontario is the

hub of the Canadian publishing industry; 83 per cent of all Canadian books sold in Canada and 98 per cent of those in English are published in Ontario.[10]

The publishing industry in the early 1980s

In the later 1960s the Ontario government re-organized its school boards and eliminated grants tied to textbook purchases. The market for locally published educational books began to shrink as required curricula were phased out and American publishers directed their marketing efforts at Canadian schools. After flowering under government nourishment in the 1970s, the Canadian book-publishing industry endured a disastrous period in the early 1980s. As the recession deepened, more problems surfaced and several firms failed.[11]

In the first half of 1983, four Ontario book publishing houses went bankrupt and two ceased operations. In May, the ODC put both Clarke Irwin and Personal Best Sellers into receivership and paid their guaranteed loans of $1.5 and $0.175 million respectively. Personal Library also went into receivership and Fleet Books was shut down as unprofitable. McClelland and Stewart, the largest publisher of Canadian books, was forced to hold a 'fire sale' of books to avert a cash-flow crisis.[12]

PROBLEMS AT CLARKE IRWIN

As the textbook market shrank, Clarke Irwin needed a replacement for this lucrative business. The company changed its emphasis and concentrated on publishing trade books for the general public. In order to broaden its publishing base, Clarke Irwin was granted a $638,000 loan guarantee from the Ontario government in April 1972. The firm was not able to make significant advances in the trade book market.[13] Clarke Irwin concentrated on importing British books in the 1970s, but their importance declined as Canadian interest shifted to US books. As a result, the company had to depend more on its own book list.[14]

Under William Clarke Jr.'s guidance, the company survived several cash-flow crises, depending on the ODC for its line of credit.[15] By December 1980, Clarke Irwin had obtained $1.5 million in loans guaranteed by the ODC and substaintial bank loans which were not guaranteed. The guaranteed loans were far in excess of the $250,000 limit and, except for McClelland and Stewart, much in excess of guarantees provided to any other publishing firm.[16]

At the start of 1983 Clarke Irwin had fifty employees, published the books of 350 authors and was the Canadian distributor for several client publishers.[17] Over $500,000 was owed to client publishers, including Lorimer, Douglas and McIntyre, Key Porter, and Kids Can Press. There was considerable concern that the collapse of Clarke Irwin would have a 'domino' effect, and damage the financial viability of these client publishers.[18]

In January 1983, Clarke Irwin lost a major foreign publishing group, eliminating a stable source of revenue. The publishing group, Britain's Bodley Head, Jonathan Cape, Chatto and Windus, cited 'fulfilment problems' at Clarke Irwin as the reason for changing distributors. In the same month, Clarke Irwin reported large losses for the year ending 31 January 1983.[19]

Clarke attributed these recent financial problems to high interest rates ($300,000 in annual borrowing costs), the recession, and the expense of converting the company from its specialty of publishing textbooks to publishing trade books. He projected more profitable performance in 1983 and 1984, based partly on the expansion of the firm's book list. He had acquired the Canadian trade list of Fleet Publishers (the Thomson group had folded this firm in early 1983). Further improvement was expected to come from the recent acquisition of the US children's book agency Dial Press.[20]

James Ramsey, deputy minister of citizenship and culture said that there were serious problems within the publishing industry, but that other publishers have 'met the challenge of the market place.'[21] Andrew Croll, executive director of the ODC, stated that 'Clarke Irwin is dangerously overextended and its problems appear to be more severe than those of its counterparts.'[22] There are several suggestions in newspaper articles that Clarke Irwin was performing badly as a result of poor management. A colleague of William Clarke (who asked that his name be withheld) stated that although Clarke is devoted to the firm and is a workaholic, his attention has been misdirected. 'In the last two years he concentrated on computer programming. Putting in a computer is a tough job and your problems are compounded when the head man does it himself.' Clarke Irwin lost its data-processing manager at the same time that a new computer was installed. When deliveries started falling behind, William Clarke became pre-occupied with the computer system. It was also suggested that Clarke Irwin had to purchase Fleet's product because there had not been sufficient development of Canadian material.

With low sales revenue, funds to commission new books were not available and consequently new sales were not forthcoming.[23]

Clarke Irwin's top writer, Timothy Findlay, blamed Clarke Irwin's difficulties on the Ontario government in a speech delivered at the tenth anniversary of the Writers' Union.[24] One article suggested that over the decade Ontario government personnel had changed and the new people were 'less committed to the book publishers development program, or at least to Clarke Irwin.'[25]

Receivership

William Clarke Jr. claims that Clarke Irwin had its most profitable quarter ever in the spring of 1983. Clarke had been out raising money, making management improvements and acquiring Fleet and Dial Press. In his view, the situation had 'turned around.' He also insists that the firm made an operating profit from 1979 to 1981, losing money only in 1982 when sales volume was poor (see Table 18).[26]

Ontario government representatives did not share the president's opinion; they concluded that the firm's current operations were not financially viable. Andrew Croll stated that Clarke Irwin had had nothing but disastrous losses for the last few years (citing a $0.5 million loss in 1982) and the only thing looking up at Clarke Irwin was their projections. He said, 'We could see no change in the foreseeable future except that as the company deteriorated, the value of its assets was being eroded.' He also claims that the CIBC wanted to call the $1.5 million loan in the summer of 1982 and wanted further ODC guarantees.[27] The ODC refused to provide more assistance until the company solved its financial difficulties.[28] Woods Gordon consultants were called in to study the firm. According to William Clarke Jr., the consultants were supposed to be 'in and out' but stayed for five months. He claims that their report presented an extremely distorted view of the company. Woods Gordon concluded that 'Clarke Irwin does not possess the managerial strength, marketing direction, organizational effectiveness nor the momentum needed to operate effectively in the short term and to survive in the long term.'[29]

At the end of April 1983, the CIBC called its loan. On 10 May, the ODC paid the bank and took over the total debt of Clarke Irwin which was in excess of $1.5 million. James Ramsey of the Ministry of Citizenship and Culture denied reports that Premier William Davis had refused to see

Clarke or that he had said 'the country can live without Clarke Irwin.' Fourteen writers are said to have asked Premier Davis to apply 'his most serious personal attention' to solving the problem.'[30] The Association for Canadian Publishers said that 'because of the Ontario government's commitments to Canadian publishing, it is hopeful the company will return as a vital, independent Canadian publisher.'[31]

On 18 May 1983 the Ministry of Citizenship and Culture and the ODC appointed Price, Waterhouse Ltd. as receiver-manager for Clarke Irwin. They immediately changed the locks, began patrolling the corridors, argued with Clarke over opening his personal mail and refused to let him continue his involvement with computer programming.[32] The receivers continued to operate the firm while looking for a buyer. The Ontario government felt that a sale 'offers the best chance to resolve the company's longstanding difficulties.'[33]

No time limit was placed on the involvement of Price, Waterhouse Ltd. They were to remain as long as there was a chance that a buyer could be found. The ideal buyer would be a Canadian firm willing to continue Clarke Irwin's publishing program and its trade-publishing activities.[34] The Ontario government assured unsecured creditors that their position would not be affected by favouring a Canadian buyer. The ODC promised to take less from the sale of assets, if necessary. This unfortunately did not imply that they would receive any payments. The government would also consider paying the claims of publishers for whom Clarke Irwin acted as distributor to prevent the domino effect.[35]

Sale

During the receivership there were twenty-five bids for Clarke Irwin.[36] On 18 June 1983 Price Waterhouse sold the firm to the Book Society of Canada which is located in Agincourt, Ontario and has twenty-three employees. The president is John Irwin, first cousin of William Clarke Jr. and the son of one of the original founders of Clarke Irwin. No consortium was needed to accomplish the purchase, which did not include Fleet books or the Clarke Irwin office building. The purchase price was not revealed, hence it is not possible to determine the extent of the loss incurred by the government.

The Book Society, which specializes in textbooks, may disappear as a separate entity; the new corporate structure was to operate under the name and imprint of Clarke Irwin. The new owners kept fifteen Clarke

TABLE 18
Clarke Irwin – sales volume 1979-82

Year	Sales volume
1979	$2,900,000
1980	2,900,000
1981	3,300,000
1982	2,900,000

SOURCE: Steed, Judy (1983) *Globe and Mail*, 18 June.

Irwin employees but William Clarke did not stay. All receivables were purchased and all outstanding contracts for work in progress were dealt with; some were honoured and others were bought out. John Irwin also plans to continue the emphasis in textbook publishing and to increase its trade publishing.[37]

The withdrawal of government support

There are several possible reasons for the withdrawal of government support from Clarke Irwin. It may have been part of a general shake-down and reduction in the publishers' support program; Personal Best Sellers was also forced into receivership by the ODC a few weeks later.[38] On the other hand, the ODC may have found William Clarke unco-operative and concluded that his management techniques contributed to the poor performance. A further possibility is that the company's book catalogue was thin on Canadian material and judged by the government to contribute little to Canadian culture.

In addition, there was a lack of communication between Clarke Irwin and the Ontario government. Government representatives were not aware of recent corporate aquisitions:

> By the time the ODC put him in receivership, Bill Clarke wasn't in touch with anyone at the ODC and had only distant relations with people in the Ministry of Citizenship and Culture. In April, when Clarke Irwin surprised the whole industry by buying the assets of the defunct Fleet Publishing . . . the people at the ministry learnt about it by reading the *Globe and Mail*.[39]

APPENDIX: CHRONOLOGICAL ORDER OF EVENTS

1965
William Clarke formally joined the firm.

April 1972
Clarke Irwin received a $638,000 Ontario government loan guarantee.

1978
The ODC introduced a $250,000 ceiling on loan guarantees under the Book Publishing Development Program

December 1980
Clarke Irwin loan guarantees reached $1.5 million.

1981
William Clarke became president.

January 1982
ODC claimed that Clarke Irwin reported substantial losses although William Clarke denied this.

Summer 1982
CIBC informed the ODC that it would call Clarke Irwin's loan if the situation did not improve and if the ODC did not extend further guarantees.

December 1982
Woods Gordon consultants began a five-month investigative analysis of the publishing industry with special emphasis on Clarke Irwin.

January 1983
Clarke Irwin reported substantial 1982 losses and lost a major British publishing group because of fulfilment problems.

Spring 1983
Clarke Irwin acquired Fleet Books and Dial Press.

28 April 1983
The CIBC called its $1.5 million loan.

10 May 1983
The ODC paid the CIBC $1.5 million.

17 May 1983
Price Waterhouse Ltd. was appointed as receiver-manager.

June 7 1983
Announcement that the Book Society of Canada Limited purchased substantially all of the business of Clarke Irwin.

NOTES

1 As Clarke Irwin is a privately owned firm, financial data was not directly available. All of the financial information mentioned in this case study was obtained from possibly unreliable newspaper articles.
2 Adachi, Ken (1983) 'Down for the count' *Toronto Star* 19 May; Godfrey, Stephen (1983) 'Buyer sought for publishing company – Clarke Irwin placed in receivership by Ontario' *Globe and Mail* 19 May; Silversides, Ann (1983) 'Clarke Irwin creditors assured position will not be weakened' *Globe and Mail* 19 May; Steed, Judy (1983) 'Clarke Irwin sold to son of founder' *Globe and Mail* 18 June.
3 Adachi (1983) op. cit.; Godfrey (1983) op. cit., Silversides (1983) op. cit.
4 Adachi (1983) op. cit.; Godfrey (1983) op. cit.; Silversides (1983) op. cit.; Perry, Robert (1983) 'Tough story for book publishers' *Financial Post* 28 May, Steed (1983) op. cit.
5 Steed (1983) op. cit.; Adachi (1983) op. cit.
6 Perry (1983) op. cit. 'A final chapter' (magazine article with no reference) 30 May.
7 Perry (1983) op. cit.
8 Ibid.
9 Adachi (1983) op. cit.; Godfrey (1983) op. cit.; Silversides (1983) op. cit.; Perry, op. cit., 30 May 1983; Adachi, Ken (1983) 'Clarke Irwin book imprint will survive' *Toronto Star*, 19 June.
10 Perry, op. cit., 30 May 1983; Steed (1983) op. cit.
11 Atwood, Margaret (1977) 'An important book for many reasons'. *Financial Post* 12 November; Perry (1983) op. cit. 28 May; Steed (1983) op. cit.; Adachi (1983) op. cit. 19 June.

12 Perry, op. cit., 30 May; Adachi (1983) op. cit. 19 June.
13 Adachi (1983) op. cit. 19 May; Godfrey (1983) op. cit.; Silversides (1983) op. cit.; Adachi (1983) op. cit. 19 June.
14 'Decline and fall'. *Saturday Night* August 1983, pp. 5-7.
15 Adachi (1983) op. cit. 19 May; Godfrey (1983) op. cit.; Silversides (1983) op. cit.
16 Ibid.; Perry (1983) op. cit. 28 May.
17 Perry (1983) op. cit. 28 May.
18 Steed (1983) op. cit.; Adachi (1983) op. cit. 19 June.
19 Adachi (1983) op. cit. 19 June; *Saturday Night* op. cit.
20 Perry (1983) op. cit. 28 May.
21 Adachi (1983) op. cit. 19 May; Godfrey (1983) op. cit.; Silversides (1983) op. cit.
22 Adachi (1983) op. cit. 19 June.
23 Adachi (1983) op. cit. 19 May; Godfrey (1983) op. cit.; Silversides (1983) op. cit.; Steed (1983) op. cit.; *Saturday Night* op. cit.
24 Perry (1983) op. cit. 28 May.
25 *Saturday Night* op. cit.
26 Steed (1983) op. cit.
27 Ibid.
28 Perry (1983) op. cit. 28 May.
29 Steed (1983) op. cit.; *Saturday Night* op. cit.
30 Adachi (1983) op. cit. 19 May; Godfrey (1983) op.cit; Silversides (1983) op. cit.; Steed (1983) op. cit.
31 Steed, Judy (1983) 'In Canada, book publishing is a perilous business where few can survive without aid – down but not out'. *Globe and Mail* 28 May.
32 Adachi (1983) op. cit. 19 May; Godfrey (1983) op. cit.; Silversides (1983) op. cit.; Steed (1983) op. cit. 18 June.
33 Perry (1983) op. cit. 30 May.
34 Perry (1983) op. cit. 28 May.
35 Steed (1983) op. cit. 28 May.
36 *Saturday Night* op. cit.
37 Ibid.
38 Perry (1983) op. cit. 30 May.
39 *Saturday Night* op. cit.

8
Whistler Village Land Company

INITIAL DEVELOPMENT AT WHISTLER

Seventy-five miles north of Vancouver, BC, accessible via Highway 99, is the Resort Municipality of Whistler. The focus of the municipality is Whistler's Village Centre developed by the Whistler Resort Association using primarily private capital generated from the sale of land by the municipally-owned Whistler Village Land Co. Ltd. The largest skiing-recreational complex in Canada serves the skiers of Whistler and Blackcomb Mountains. Whistler Mountain was initially developed by Garibaldi Lifts with the installation of a four-passenger gondolas and a double chair-lift in the winter of 1965-66.[1] The mountain was believed to be ideal for development, boasting the highest vertical drop in North America. This and its proximity to Vancouver made the area a tremendous success in the 1960s and 1970s.

The 1960s was a period of sporadic, uncontrolled development. Highway 99, despite repeated work by the provincial government, deteriorated and was often closed completely by storms. Whistler was a 'community' of squatters, weekender cabins, two gas stations, and four hotels in various states of disrepair. Local government was provided by the Chamber of Commerce which did little to prevent the area from becoming a 'ski slum' and a 'hippy haven.'

In the early 1970s Al Raine, husband of Olympic skier Nancy Greene and an avid skier at Whistler, took an interest in its development.[2] He persuaded Robert Williams (NDP), then the BC minister of lands, forests and water resources, to support a well-planned development of the area. The plan was supported by permanent residents who were concerned

that the proliferation of private water systems and septic tanks posed a serious pollution threat to the Alta Valley lake and river systems. In April 1974 L.A. Williams, MLA for the area, urged the incorporation of Whistler so that the community could enjoy a formal administration and receive assistance from the provincial government for the provision of necessary sewage facilities. The government's first response was to freeze land development at Whistler under environment and land use committee regulations.[3] This was followed by a Department of Municipal Affairs community development study which was released in March 1975. The report identified a number of local problems such as road maintenance and water pollution and recommended that 'Whistler should be reserved for British Columbians for their own recreation . . . the area shouldn't be developed into another St. Moritz, Aspen, or Sun Valley. It should not become a focus for the international jet set . . . but in fact should become a facility for British Columbians.'[4] Debate centred on whether this was an economically viable position since Whistler needed seven-day use to be a success, and the majority of use from British Columbians occurred on weekends.

On 11 June 1975 the first reading of the Resort Municipality of Whistler Act took place in the legislature. The government-sponsored study had been accepted as the basis for policy despite the negative reaction of the Whistler Development Association, which represented developers and landowners keen on developing the resort into a world-class facility. On 24 June 1975 James Lorimer, then NDP minister of municipal affairs, presented the central issue in the Act as the development of a unique community in an area with few permanent residents and a large winter weekend population.[5] The area needed the facilities to meet the requirements of a large population, but the permanent residents could not be expected to bear the costs alone. Since the provincial government owned a high percentage of the land in question, the issue was the investment of provincial funds for the benefit. The NDP wanted the provincial government to be integrally involved in Whistler's development. The government had therefore decided to appoint one representative to Whistler Council to represent wider interests; the other three aldermen and the mayor would be elected. The appointed alderman would represent the interests of those who use Whistler, but have no votes there, would serve as a liaison between the Whistler Council and the provincial government, and would be directly reponsible to the minister of municipal affairs. Lorimer assured critics that the

appointment of an alderman would not serve as a precedent for provincial government interference in municipal affairs, nor would it signal an erosion of local autonomy. The Act passed on 25 June 1975, based on the provincial government's intention to proceed with the single town centre and to directly fund $10 million in municipal facilities. Sales of land in the town centre would be used to recover all public costs. The Act called for the creation by the municipality of the Whistler Resort Association to promote and aid in the development of the resort. The Whistler Village Land Company has controlled most property transactions.

THE DEVELOPMENT OF A RESORT COMMUNITY

The appointment of Al Raine as the provincial co-ordinator of ski development in April 1974 and as alderman in June 1975 signalled the renunciation of the premise of the Department of Municipal Affairs study that Whistler be reserved for British Columbians. Raine's goal for Whistler was a 'world-class destination resort' which, to balance the books, would also attract visitors in the summer.[6] His development plans continued uninterrupted following the December 1975 defeat of the NDP by William Bennett's Social Credit Party.

One of Raine's first moves as provincial co-ordinator of ski development was to persuade the province to limit logging in the Blackcomb-Whistler area while its potential for ski development was evaluated.[7] The base of the two mountains was an ideal site for a town centre to act as the focus of the resort. Whistler's founding mayor, Pat Carleton, and the Whistler council went to Aspen and Vail to learn how to create a top resort. The province announced a public proposal call for the development of ski lifts in Blackcomb Mountain. It was intended that a key feature of the development process at Whistler would be the involvement of residents. The contract to develop Blackcomb Mountain was awarded to Fortress Resorts Ltd., a company formed by the Aspen Skiing Corporation in partnership with the Federal Business Development Bank.[8]

In January 1978 the Whistler town plan was announced by the provincial minister of municipal affairs. The town was to be located on 135 acres of Crown land donated by the provincial government to the municipality for subdivision and resale. In April 1978 the Whistler Village Land Company was incorporated to control land transactions, and the Crown lands were transferred to the company.[9] To create a

resort village at the base of Whistler North Side and Blackcomb Mountain, the municipally-owned Whistler Village Land Co. Ltd. began to sell the parcels of Crown land. They were to be sold at a profit to recover some of the servicing costs of the resort and help finance a number of facilities, including a convention centre, a day lodge, and a parking structure. The cash-flow situation was aided by $10 million 'loan' through the Tourist Industry Development Subsidiary Agreement (TIDSA), a joint federal-provincial tourist industry program. The loan was to be forgiveable upon completion of resort development. To date, the Whistler Village Land Co. Ltd. has not been required to pay for the land or to repay the $10 million.

Developers and speculators moved into Whistler attracted by MURB tax shelters (money borrowed for investment qualified as a tax deduction.)[10] Over the period 1979-87, approximately $342 million in private and public money has been earmarked to develop Whistler and Blackcomb. By 1981 a well-planned town had 'sprung out of nowhere.' Whistler Village enjoys the facilities (hotels, restaurants, car-rental agencies) of a viable community although it still lacks a bank and a library. Blackcomb and Whistler are keenly marketed, each with 'snow hosts' to organize tours and special events. The two mountains can lift 13,000 skiers a day on their combined lift capacities.[11] The transformation of Whistler has proceeded rapidly, although the real-estate and development boom collapsed in early 1982.

Problems with development

Central to Whistler's development plans were a major full-service hotel, a day lodge, and a sports and convention centre. The golf course, which was to increase the resort's attractiveness to summer visitors, opened in June 1983. In the early years of Village development (1978-80), three provincial deputy ministers (Municipal Affairs; Lands, Parks and Housing; and Lands, Forests and Water Resources) met as an informal steering committee which acted as a liaison between the Whistler Council and the provincial government. The provincial government supported development with the rationale that Whistler was an example 'where government can take the lead and make it happen, where we can attract private enterprise to come in and help build this province and in the process provide thousands of jobs for young people.' Bill

VanderZalm, then minister of municipal affairs, estimated that development in the area would create 11,000 person-years of work.[12]

However, by early 1982 the optimistic forecasts for Whistler had proved unwarranted. In November 1981, federal Finance Minister Allan MacEachen unveiled a budget which eliminated the MURB tax shelter upon which most of the private condominium hotel investment in Whistler had been built. Buyers could no longer be found for sites, and the Whistler Village Land Co. Ltd. faced a severe cash-flow crisis. The bottom fell out of the real-estate market, which had boomed until the spring of 1981. The Whistler Village Land Co. Ltd. had not sold land since October 1981. If properties sold privately, vendors were lucky to receive half the early-1981 price.

Construction of the convention centre and day lodge continued during this period and costs rose steeply. Interest rates were also rising steadily, reaching 22 per cent in the fall of 1981. The preliminary estimate for a smaller, multi-use recreation centre was \$3.5 million. The original approved estimate for the facility was \$5.2 million. By early 1981, when it was half-built, it had cost \$6.7 million.[13] Problems were compounded by major design changes and a labour dispute in the fall of 1981.[14] Unionized labour would not permit local non-union labour to work on the same site, and restricted the temporary construction camp to unionized employees. The empty part of the camp cost the Whistler Village Land Co. Ltd. over \$20,000 per month for security and other operational, rental, and maintenance expenses.[15] As a result of this dispute the convention centre project was shut down for the winter, necessitating the storage of supplies and equipment. Startup in the spring of 1982 was expensive, and costs rose again with a new wage settlement. It became clear that the Whistler Village Land Co. Ltd. could not afford completion, and in October 1982 all work was halted and all employees laid off. It will cost at least \$5 million to complete the convention centre;[16] the day lodge was sold at a loss of almost \$500,000. The day-lodge site was excavated, filled, then excavated again at great expense,[17] due to the opening of Whistler North Side and Blackcomb lifts and the need for a ski base area for December 1980.

Lesser difficulties included the propensity of developers to fix higher rents for commerical properties. The federal government refused to pay the rent demanded for the post office in the Village but preferred to use temporary quarters three miles away. Therefore the Land Company was forced to subsidize the rent to ensure that Whistler had basic institutions

in a central location in the Village. In addition, there were allegations of a scandal; Mayor Carleton and Alderman Garry Watson were directors of the Whistler Village Land Co. Ltd. (which controlled the major commercial development of Whistler) and also were the town's municipal officers. However, following a provincial government-assisted audit no evidence of misuse of funds was discovered.[18]

In January 1982 Ken Browes was appointed to the board by Attorney-General Allan Williams, also the MLA for the area, to try to assist the Whistler Village Land Co. Ltd. and the Whistler Resort Association. Browes contended that Carleton and Watson (directors of the resort association and the Land Company because they were municipal officers) did not have sufficient expertise, and that therefore the managers of the Whistler Village Resort Association had not had adequate guidance from the board of directors.[19] Browes then requested that the BC government take over the company.

Al Raine resigned as executive director of the Whistler Resort Association in the spring of 1982 citing ill-health; he had previously resigned as alderman (December 1981) and Provincial Ski Co-ordinator (1979). He was replaced by Earl Hansen, who announced that the Whistler Resort Association was short of sufficient capital and was turning all its operations back to the municipality. Whistler began to attract negative publicity which was fueled by a local effort to save the development by bringing in legalized gambling The *Vancouver Sun* decried the 'big profits the get-rich-quick artists made during Whistler's boom,' and warned the resort not to expect a bailout.[20] 'British Columbian taxpayers have already invested plenty in Whistler's playground for jetsetters . . . without seeing much return on their investment so far.' VanderZalm, the minister of municipal affairs, announced that the Whistler Village Land Co. Ltd. did not merit special treatment and that the government could 'not bail them out any more than we can bail out a private developer.'[21] However, Mayor Carleton and the WVLC board members continued to lobby for a bailout as they had done since April 1982.

In October 1982 the land company announced that it was out of money and \$6.5 million in debt. It had \$27 million in contingent liabilities, including \$4 million owed to the Royal Bank of Canada and \$1.5 million to the Yorkshire Trust.[22] On 5 January 1983 John Johnston, deputy minister of lands, parks and housing, announced that a crown corporation would take over.

THE BAILOUT

WLC Developments Ltd. was created under the BC Company Act in January 1983 and assumed the liabilities and bank debt of the Whistler Village Land Co. Ltd. At a cost of $1, the BC government purchased the 100 outstanding shares of the land company and assumed control.[23] Lands, Parks and Housing Deputy Minister John Johnston was made the new corporation's interim president, responsible to the minister, the Honourable Anthony Brummet. At this time the legislative assembly was not in session, having recessed on 7 October 1982. Timing the decision to bail out with the recessing of the legislature may have been a calculated move, since in a period of recession and high unemployment a bailout of the 'jet set' was not likely to be politically popular. The new session was not due to commence until March 1983.

Johnston rationalized the takeover as a decision to protect the province's $20 million investment (the value of crown land and the province's share in a $10 million federal-provincial grant) and to ensure the confidence of private interests in the idea of a year-round resort.[24] The provincial government was concerned with the province's credibility in the tourist industry. The government expected recovery and profit within ten years at which point the land owned by WLC Developments Ltd. would be sold to the private sector. WLC Developments Ltd. would pay all operating bills and administration costs until that time. Much was made of the assets of the land company and of the Resort Association – twenty-two hectares of developable land, a convention centre, and a golf course. Brummet claimed that the takeover prevented 'profiteering' from these assets, since 'bankruptcy or receivership would have triggered a takeover by the secured creditors, and they would have picked up millions of dollars of assets for a song.'[25] It was made public that a group of investors had offered $7 million for the land (a sum which just exceeded the value of the Whistler Land Company's debt). However, Brummet had rejected the offer claiming that the company's assets were worth three times the offer and the government was not prepared to relinquish control over the process of development.[26]

On 28 February 1983 the takeover deal was finalized, and the financial arrangements were announced. Some $9.2 million would be borrowed from the Royal Bank in the first year at bank interest rates. These funds would enable the completion of the convention centre at a

cost of $5.8 million. The government stated that it was possible, but not probable, that public funds would be used to pay off what was used of the $9.2 million.[27] Payment was postponed for three years on bank loans to the Land Company totalling $5.5 million and a further $700,000 was borrowed from the Royal Bank and Yorkshire Trust to pay 65 unnamed, unsecured creditors. The payment of $2.1 million owed by the Land Company to the municipality has been postponed until other creditors are paid.

A new nine-member board of directors of WLC Development Ltd. was appointed without any representation from the Whistler Council.[28] Mayor Mark Angus objected that he, or some member of council, should be on the board to represent the interests of the municipality.

Reactions to the bailout

The bailout of Whistler Village Land Co. Ltd. was not well received. BC Federation of Labour president Jim Kinnaird termed the takeover 'scandalous,' and said the rescue funds should have been used for job creation. He accused the government of 'burdening the poor to bailout the rich,' and of giving handouts to 'jet-set supporters of the Socreds.'[29]

Members of the NDP apparently regretted their early association with the development of Whistler. NDP House Leader Frank Howard demanded that cabinet give firm control of WLC Developments Ltd. to the Crown Corporations Committee of the provincial legislature so that all transactions could be monitored, and the initial deal reviewed.[30] Bennett refused, stating that he would not give the NDP fuel for political gain.

Political debate erupted when it was discovered that WLC Developments Ltd. had been formed without a cabinet order, but was instead incorporated as a regular private company. Since the legislature was not in session, it also had not been consulted. BC paid $1 to become the new owner and shareholder. However, the expenditure was not authorized by the legislature. Tony Brumett stated that the $1 was taken from the Crown Land Fund, a surplus fund administered by his department (Lands, Parks and Housing).[31] Withdrawal from the fund does not require a cabinet order or legislative approval. There was also a question whether WLC Developments Ltd. was actually a Crown corporation. It was established as an ordinary company under the Company Act, unauthorized by the legislature, and is therefore not subject to the same

scrutiny as a Crown corporation. The issue was marked by minimal public debate, and debate did not resume when the legislature reconvened in March 1983.

CONCLUSION

The BC government has always been involved in the development of Whistler. WLC Developments (managed by the provincial government) is intended to restore the confidence of investors and creditors, and help Whistler overcome the crisis precipitated by inexperienced management, rising interest rates and the onset of recession, and the resultant severe cash-flow problems. WLC Developments has been granted implicit loan guarantees in that the government assumed the liabilities and the bank debt of the Whistler Village Land Company. While the NDP initiated government involvement in Whistler's development, its ideas were taken over and implemented by Bennett's Social Credit party, which although philosophically opposed to government intervention, has been similarly committed to Whistler's tourist-attracting abilities.

NOTES

1 Michael Bliss (1983) 'The Mountain and the Valley'. *Saturday Night* January.
2 Ibid.
3 *British Columbia Debate of the Legislative Assembly* 3 April, 24 June, 1974.
4 Ibid. 12 March 1975.
5 Ibid. 24 June 1975.
6 Bliss (1983) op. cit.
7 *British Columbia Debates* 19 June 1975.
8 Bliss (1983) op. cit.
9 Resort Municipality of Whistler sole shareholder of Whistler Village Land Co. created April 1978 (mayor and alderman are directors); assets transferred to WLC Developments Ltd., March 1983; Whistler Resort Association – Marketing arm of the resort created June 1975 (all businesses in Whistler Village must be members).
10 *Vancouver Sun* 24 January 1983.
11 Bliss (1983) op. cit.
12 *British Columbia Debates* 19 March 1981.
13 Bliss (1983) op. cit.

14 *Vancouver Sun* 24 January 1983.
15 The union's position was supported by the British Columbia Labour Relations Board.
16 *Vancouver Sun* 8 January 1983.
17 *Vancouver Sun* 24 January 1983.
18 Ibid.
19 *Vancouver Sun* 14 January 1983.
20 Bliss (1983) op. cit.
21 *Vancouver Sun* 8 January 1983.
22 Ibid.
23 *Globe and Mail* 7 January 1983.
24 *Vancouver Sun* 8 January 1983.
25 *Globe and Mail* 15 January 1983.
26 *Vancouver Sun* 14 January 1983.
27 Ibid., 25 March 1983.
28 Ibid., 5 May, 1985.
29 *Financial Post* 22 January 1983.
30 *Vancouver Sun* 19-20 January 1983.
31 Ibid.

9
Canada Cycle and Motor Company Limited

BACKGROUND

Canada Cycle and Motor Company Limited (CCM) was established in September 1899 with the issue of $2 million in shares. The company was formed from the bicycle and parts businesses of Massey-Harris Company Limited, H.A. Lozier and Company, Welland Vale Manufacturing Company Ltd., Godd Bicycle Company Limited, and Gendron Manufacturing Company Limited.[1] (Appendix 9A provides a complete chronology of CCM.)

In 1905 CCM manufactured the first Canadian-made automobile, the Russel. After World War I, the company specialized in bicycles and sporting goods and grew to become Canada's dominant manufacturer of these items.[2]

In the mid-70s CCM employed 1,150 workers, 700 in its 265,000 square foot Toronto plant and 450 in its 130,000 square foot St. Jean, Quebec plant. The Toronto plant, located on Lawrence Avenue West in Weston, produced bicycles, exercycles, skate blades, and hockey helmets. The complete line of hockey equipment was produced in the St. Jean plant.[3]

Until the late 1970s CCM was a wholly owned subsidiary of Levy Industries Limited of Toronto. Levy was purchased in the spring of 1969 by Seaway Multicorp Limited, another Toronto holding company. In that purchase Seaway was reported to be primarily interested in acquiring CCM, but Levy would not part with CCM except as part of the total group of Levy companies.[4] Levy Industries also operates auto-parts manufacturing and distributing companies in Canada, the United

States, and Europe, owns Levy Services Industries, a warehouse firm, and Premium Forest Products Limited, the largest producer of doors for the Canadian building industry. It also has subsidiaries which manufacture farm equipment and aircraft components.[5] As of August 1977 both Levy Industries and Seaway Multicorp Limited were controlled by the Levy family.[6]

The early 1970s

In the early 1970s, CCM enjoyed receptive markets for its products, both at home and abroad. In 1970, the Targa, a tough, popular-priced bicycle was introduced and became a tremendous sales success. In 1971, CCM began exporting bicycles to the United States; distribution had previously been 100 per cent Canadian.[7] To meet the growing domestic and foreign demand and to produce more bicycle components, CCM went ahead in 1972 with a multimillion dollar expansion of its Toronto facility.

Total domestic unit sales were expected to increase from 0.7 million in 1971 to 1.1 million in 1972. Bicycle imports rose from 330,000 in 1970 to 488,000 in 1971. In the first five months of 1972, imports totalled 531,000 units, an 85 per cent increase over the same period the previous year. Prices on domestic and imported bicycles were comparable due to tariff protection of 18 per cent on British made units and 25 per cent on units imported from other countries. Of all imported bicycles, Japan held the largest share at 33 per cent, followed by Britain (15 per cent), Poland (10 per cent), France (10 per cent), West Germany (8 per cent), and Taiwan (8 per cent).[8]

In 1974, costs for quality European and Far Eastern manufacturers had risen to nearly equal those of their North American counterparts. Also, demand had increased drastically since the 1973 energy crisis causing a 'bicycle market boom'. CCM seized the opportunity and began exporting bicycles to Britain, Nigeria, Jamaica, and Australia.[9]

Until the summer of 1972, CCM had been the lone domestic bicycle manufacturer. In the week of 26 August, Raleigh Industries Limited broke ground for a $1.3 million addition to its Waterloo, Quebec plant to open a new bicycle assembly line. The plant had been used previously by another British firm, Lines Brothers (of Canada), to produce metal toys. Another entrant, Sekine of Japan, was negotiating with Winnipeg-based automotive and hardware distributor, Acklands Ltd., to build a bicycle

plant in Manitoba. The Manitoba Department of Industry and Commerce was also 'making pitches' to other foreign bicycle manufacturers.[10]

PROBLEMS AT CCM

During the North American bicycle-market boom, CCM increased its business but cheaper imports also took part of the increasing market. The boom market settled down and CCM was caught overproducing while demand for locally produced machines dropped in favour of the cheaper imported models.[11]

Misjudging the market was not CCM's only mistake during this period. Quality control was practically eliminated when the bicycle plant was operating at capacity. Low capital spending allowed the plant to deteriorate; equipment and procedures became outdated.[12]

Poor marketing seems to have been the most serious problem. CCM produced fifty-eight different bicycle models, resulting in interline competition, lack of product line conformity, and dealer confusion. Deliveries were slow and relationships with retailers deteriorated.[13] Retailers complained that CCM never adhered to a definite marketing policy to enable retailers to develop long-term selling strategies. In hockey equipment and bicycles, CCM allowed some dealers to sell at low markups. CCM's strategy made a few big buyers happy but tens of thousands of small stores unhappy.[14] Retail dealers lost their trust in CCM when an attempt was made to negotiate wholesale prices separately with each dealer. Small dealers found themselves unable to compete with the CCM product sold by volume retailers who got the same bicycles for less.[15]

After three years of serious losses and cash-flow problems, fifteen of CCM's top executives were replaced. Ben Virgilio joined CCM as executive vice president on 1 April 1976. He was given a five-year contract and a mandate to turn the company around.[16]

Virgilio started upgrading equipment and manufacturing procedures. For example, skate-blade production, which had previously been done by hand, was mechanized with the help of Virgilio's experience in the auto-parts industry. The Canadian distribution system was reorganized and quality control was upgraded. Virgilio used a team approach, combining the vigour and drive of a new, young management team with the wisdom of long-time CCM executives. He also consulted frequently with both unions, the UAW and the International Woodworkers of Canada.[17]

The biggest challenge was to restore the confidence of retailers. The campaign to win back dealers began in 1977 when the entire CCM line was scrapped. Several hundred thousand dollars were spent retooling for twenty new models.[18]

Virgilio's efforts were stifled by import competition and financial difficulties. In the spring of 1977, a $6 million fire at the St. Jean plant destroyed the winter inventory of hockey equipment and resulted in major borrowing. From 10 June until August, bicycle production was decreased at the Toronto plant; two hundred workers were laid off indefinitely and another 250 workers were laid off temporarily. Only 165,000 bicycles were produced during 1977; the plant operated at 30 per cent of its 550,000 unit capacity.[19]

Serious financial difficulties

The year 1977 was a particularly bad one for Canadian bicycle manufacturers; of all bikes sold in Canada, 75 per cent were imported from Taiwan and Japan. Bikes from Taiwan and South Korea enjoyed a 16 per cent increase in market share while the market share of Canadian manufacturers declined by 7 per cent. Of the 1.1 million bikes sold in Canada, Canadian manufacturers produced only 250,000 and 346,000 were imported from Taiwan and South Korea alone.[20] The Canadian Bicycle Manufacturers Association complained to the federal government that these countries were 'dumping' bicycles in the Canadian market. In an unprecedented step, in February 1977 the federal cabinet imposed a $15 per unit surtax on bicycles from Taiwan and South Korea, pending the outcome of a Revenue Canada investigation and an Anti-Dumping Tribunal hearing. The surtax was replaced in November 1977 by a 'fair market surcharge' on bicycles imported from these two countries. The import levy was designed to keep prices higher than those of domestic products.[21] It was extremely effective in reducing import competition. Total imports dropped from 784,000 in 1977 to 240,000 in 1978. Taiwan's share of the Canadian bicycle market dropped from 45 per cent to 8 per cent.[22]

Government aid

In addition to these protective measures, CCM sought and obtained financial assistance from the government. In June 1977 the Canadian Imperial Bank of Commerce (CIBC) warned that $6 to $8 million in loans

to CCM might have to be called. This would have shut down the Toronto plant with a loss of 700 jobs. Levy Industries approached the Enterprise Development Board (EDB) (part of the federal Department of Industry, Trade and Commerce) for restructuring help. The EDB provided CCM with $8.2 million in guarantees on CIBC loans, to be used to implement the restructuring plan. In return, the EDB received the option to buy CCM. J.R. Scopick of Industry, Trade and Commerce (ITC) later claimed that the company's legal and financial advisors 'envisaged the divestiture of the bicycle and winter goods manufacturing operations over a 12-month period'.[23]

By March 1978 ITC had kept the Toronto plant open for eight months by 'bringing pressure to bear' on the CIBC. This was done on the understanding that Levy would make a serious attempt to find a buyer for CCM. The CIBC was concerned about the quality of information provided by CCM and brought in Peat Marwick Ltd. to monitor the company's day-to-day operations.[24] CCM had been losing money for five or six years and market share for bicycles had fallen from 50 per cent to less than 20 per cent. Levy Industries was reported to be asking $16 to $17 million for the company, although it had $35 million in assets. The federal government wanted both divisions sold as a single unit to a Canadian firm.[25]

Sale to Maxwell Cummings and Sons Holdings Ltd.

After discussions between Maxwell Cummings and Sons Holdings Ltd. and the EDB, it was announced on 15 March 1978, that there was an agreement in principle to buy CCM.[26] The negotiating process took three months, during which the EDB exercised its option to buy CCM and sold the firm to Cummings. This route was taken to avoid the possibility of foreign interests negotiating directly with Levy Industries. It also allowed the federal government to extract guarantees that the acquirer would maintain both divisions. Completion of the sale was announced on 29 June 1978.[27]

A key negotiating point in the sale was the extent to which the government would provide financial assistance. The banking relationship between CCM and the CIBC, which had existed since the company's formation, was terminated. The Royal Bank became the main lender with $11 million in loans guaranteed by the EDB. The overall financial arrangement included government loans to cover the cost of plant and

equipment and financing from the Royal Bank to cover inventory and accounts receivable. The purchase price was not revealed but Cummings claimed that it was 'well below' the $17 million that Levy had reportedly been asking.[28]

Maxwell Cummings and Sons Holdings Ltd. of Montreal is a private family company which began as a real-estate concern. It is now a large Canadian conglomerate with subsidiary interests in the leisure-products industry. Cummings' portfolio includes oil and gas holdings, 2,500 acres of Florida orange groves, a Texas metal fabricator, a California photo-finishing chain, a medical-technology firm and a chain of health-food restaurants in New York. It also owns land and real estate in Montreal and Alberta through Cummings Properties Limited.[29] It was Cumming's 50 per cent ownership of Empire Distributors, a Montreal bicycle and winter sports equipment importing and distribution company, that prompted the purchase of CCM. Empire imported bicycles from Japan and Taiwan and as a competitor of CCM had a 10 per cent share of the Canadian market (CCM had a 15 per cent share). The other 50 per cent of Empire Distributors was held by president Sheldon Hamer, who became the president and minority shareholder of CCM.[30]

The fit between Empire and CCM was almost perfect. Both sold to the same dealers and their product lines were complementary. The cheaper line of imported bicycles could be sold alongside the more expensive domestic bicycles produced at the CCM factory in Toronto. Hamer stated that the advantage of the CCM line was the ability to fill orders on short notice, where importers must plan a full year in advance. The acquisition also gave Cummings a full range of sports equipment. The skates and hockey equipment produced at the St. Jean plant were matched by Empire's imported Blizzard brand skis, Kastinger ski boots, and Kuusisto cross-country skis.[31]

Cummings announced that it would operate both CCM divisions and invest in new equipment for both plants. It considered introducing new products to keep the plants working steadily all year; for example, CCM could produce the previously imported Empire line of bicycles. At the St. Jean plant, new product development would include the investment of $1.5 million in machinery for moulded skates. A new national television advertising campaign was also expected to boost sales.[32]

Ben Virgilio was asked to remain with the firm. He stated that marketing was a bigger problem than capital investment. He suggested plans to increase research and development expenditures with the help

of federally funded incentive programs. The good performance of the winter line of skates and hockey equipment was to be improved by establishing new markets in Europe.[33]

In their first year, the Cummings group was able to reverse the losses at CCM (see Table 18).[34] This recovery was due in part to a sharp decline in imported bicycles as protection for Canadian manufacturers increased. In addition to the 'fair market surcharge' on bicycles from Taiwan and South Korea, new duty-valuation regulations were imposed on bicycles imported from Poland, Hungary, and Czechoslovakia. Canadian bicycle imports dropped by 50 per cent in 1978 when the new regulations took effect.[35]

THE EARLY 1980S

Further problems at CCM

The domestic bicycle market became more competitive in the early 1980s with a contraction in unit sales and the appearance of new entrants. New competitors included Beekay Corporation and Pro Cycle. Raleigh had become a serious challenger to CCM in unit sales volume. The bicycle market was down to 850,000 to one million units per year, compared to the peak of 1.3 million in 1974.[36]

Although the Canadian sporting-goods industry was enjoying rapid growth, it was suggested that the retailers and distributors reaped most of the profits. Domestic manufacturers faced handicaps; the small Canadian market and import competition. Bicycle manufacturers faced a serious problem; the need for a domestic alternative to increasingly expensive, high-quality Japanese components.[37] CCM was in worse shape than most. Its bicycle plant was in need of a major overhaul. Management blamed poor performance on the old plant, noncompetitive wage rates, and high interest rates. Raymond Dutil of Pro Cycle claimed that the new owners lacked manufacturing expertise.[38] Operating results for 1981 and 1982 are given in Table 19.[39]

In addition to poor market conditions, CCM had firm-specific problems in 1982. Early in the year, a proposal to purchase Raleigh Industries fell through because CCM was unable to obtain financing. The Boston-based Bank of New England refused to renew the $4 million line of credit extended to CCM to finance exports to the United States. The company was able to cover the loss of credit only by offering personal guarantees to the Royal Bank. CCM also tried, unsuccessfully, to raise

TABLE 18
Sales and profitability 1979, 1980

Year ended	Sales volume	Profit/(loss)
30 Sept. 1979	$47,805,560	$(562,298)
30 Sept. 1980	57,922,116	1,174,258

SOURCE: Consumer and Corporate Affairs.

TABLE 19
Sales and profitability 1981, 1982

Year ended	Sales volume	Profit/(loss)
30 Sept. 1980	$60,979,405	$(1,774,744)
30 Sept. 1982*	59,622,187	(4,300,000)
*(unaudited)		

SOURCE: Consumer and Corporate Affairs.

$10 million in new equity, a good part of which was to be injected by its principal shareholder, Cummings.[40]

In 1982 CCM also had serious labour-relations problems in the Toronto plant. After being asked for concessions amounting to an estimated 34 per cent or $4 per hour in wages and benefits, the workers went on strike for two and a half months. At the end of July, the company had to decide whether to settle the strike or jeopardize bicycle orders for the 1983 spring and summer market.[41] On 10 August the 190 workers who had survived pre-strike layoffs accepted a three-year contract. They received a wage increase of $2.60 to $3.00 per hour and improved benefits. The contract improved their cost-of-living allowances and benefits and provided for a three per cent wage increase over cost-of-living allowances in the third year. After this settlement, CCM's labour costs were 80 to 100 per cent higher than those of its bicycle competitors.[42] Management claimed that this expensive settlement made it difficult to attract new investors at a time when the firm was badly in need of an infusion of new capital. During this period, CCM made efforts to obtain financial assistance from the Province of Ontario. The Ontario government was not interested in the ailing firm.[43]

Bankruptcy and the sale of assets

On 14 October 1982 CCM filed a holding proposal in the Supreme Court of Ontario under Part III of the Canadian Bankruptcy Act. CCM sought and received a moratorium on its debt payments until 31 January to allow time for an attempt to restructure its debt obligations under court supervision.[44] The submission of a definitive proposal depended on CCM's success in obtaining investment capital, renegotiating the terms of its indebtedness to the EDB, and renegotiating the collective agreement with its Weston plant employees. Richter and Partners Inc. of Toronto was named interim receiver. The company continued to operate and to fill customer orders.[45]

The financial situation was bleak. CCM owed creditors almost $55 million. At 19 January 1983, book value of assets was $36 million but liquidation value was estimated to be only $27.4 million (see Table 20).[46]

The principal secured creditor was the Royal Bank, with a claim of $33.5 million secured by:

1 Registered general assignment of book debts.
2 Section 178 of the Bank Act.
3 A trust deed of hypothec, mortgage and pledge.
4 A fixed and floating charge debenture.

Of the $33.5 million, $11 million was guaranteed by the EDB. The EDB also had $4 to $5 million in secured claims, which were later transferred to unsecured status; various trade vendors had secured claims of $150,000. The contingent claims were product-liability actions. All but one was adequately covered by insurance; a $12 million suit, Steele vs. CCM, for which coverage was limited to $3 million, leaving potential exposure of $9 million.[47]

In addition to the above claims, the UAW was a contingent claimant but was not listed as a creditor. Representing certain employees, the union filed a claim in the total amount of $7.2 million, of which $4 million was being claimed as secured, $3.2 million as preferred, and $1000 as unsecured.[48]

CCM made a serious attempt to restructure its debt. The federal Department of Justice ruled that an attempt to convert EDB loan guarantees into preferred-share debt was illegal. CCM was also unable to either ob-

TABLE 20
CCM's total liabilities

Liabilities	
Secured	$37,245,355.56
Preferred	1,163,955.08
Unsecured	3,795,722.69
Contingent	12,664,011.00
	$54,869,044.33

SOURCE: Consumer and Corporate Affairs.

tain the new share capital needed for reorganization or renegotiate with the UAW.[49]

While various offers were received to purchase certain of CCM's assets, no investors came forward. On 8 December 1982 CCM accepted an offer from Gestion R.A.D. Inc. for its inventories, fixed assets, and intellectual properties. The sale to Gestion was completed on 22 January 1983 (see Table 21).[50]

Gestion then sold the hockey division on a going-concern basis to Sport Maska Inc., a Quebec-based manufacturer of athletic uniforms. Pro Cycle Inc., also of Quebec, bought the assets of the money-losing bicycle division. The immediate plan was to use only the CCM plant assets for parts, but it also bought the right to use the CCM name in the future.[51]

The proceeds from the sale of assets, together with the value of accounts receivable, were not sufficient to retire CCM's indebtedness to secured lenders. Thus CCM was unable to file an amended proposal. Richter and Partners recommended that the Supreme Court of Ontario in Bankruptcy not approve the proposal. On 24 January the Court ordered that the proposal not be approved.[52]

The extension and withdrawal of government support

Government involvement had begun in the spring of 1977 when the CIBC warned that it was about to withdraw $6 to $8 million in loans to CCM. As this action would have resulted in the loss of 700 jobs at the Toronto plant, the EDB guaranteed $8.2 million in loans in return for the option to buy CCM. This option and further financial support were later used to ensure that the firm remained in Canadian hands and both plants continued operating.

TABLE 21
Components of CCM's purchase price

Summer goods inventory (full value based on auditor's opinion	$3,798,000
Winter goods inventory (50¢ on the $1 based on CCM's book value to a maximum of $3 million)	3,000,000
Fixed assets	1,750,000
Intellectual properties	250,000
TOTAL PURCHASE PRICE	$8,798,000

It may be that adverse circumstances (i.e., the St. Jean fire and the slow arrival of protection from imports) masked real firm-specific problems at CCM. The company may have argued convincingly that were it not for circumstances beyond management's control, government support would not be necessary. A major problem was that as protection increased, so did the number of new domestic competitors with modern plants and manufacturing procedures.

A less-fortunate bicycle manufacturer downplayed the job-saving argument and contended that CCM received government support because it was a subsidiary of Levy Industries, a Toronto-based holding company with longstanding ties with the federal government and many foreign governments. Three aspects of the loan guarantee for CCM were cited as being unusual:[53]

1 A few months earlier, ITC had put the bicycle industry on the sensitive list because of a softening in the market.

2 The EDB moved on twenty-four hours' notice when the Levy family appealed for help, claiming that 2,500 jobs would be lost if there was a 'domino effect' on other Levy companies.

3 CCM was given special treatment; 'the EDB had overruled the civil servants in the ITC and had bypassed the usual procedures . . . some ITC officials did not support the assistance package developed for CCM. They believed the company's troubles resulted from bad management and poor marketing policies'.

If government support for CCM was based on the influence of the Levy family, this could explain its withdrawal after the Cummings purchase. However, it is clear that government support was not withdrawn precipitously. In the face of poor performance, new capital was not subsequently made available by the new owners, perhaps because they were not willing to throw more good money after bad. The fact that the conversion of EDB loan guarantees into preferred share capital was ruled illegal by the federal Department of Justice implies that the EDB was willing to support the restructuring proposal. CCM's financial position in 1982 was not attractive to new investors.

In addition to the poor financial and market position of the company, a good argument could be made for the withdrawal of support based on employment levels. The St. Jean plant had much higher employment in late 1982; 450 workers compared to 190 at the Toronto plant. The St. Jean jobs were not in need of protection; the division was profitable and could be sold on a going-concern basis.

APPENDIX 9A: CHRONOLOGICAL ORDER OF EVENTS

1899
Canada Cycle and Motor Co. Ltd. founded.

1905
CCM produced first Canadian-made car, the Russel.

Post WWI
CCM specialized in bikes and sporting goods; Canada's only domestic manufacturer.

Spring 1969
Seaway Multicorp Ltd. takeover of CCM owner Levy Industries Ltd.

1971
CCM begins exporting bicycles to the United States; previously 100 per cent Canadian distribution.

Summer 1972
CCM plans expansion of its Toronto bicycle-manufacturing facility.

26 August 1972
Raleigh Industries breaks ground for Canadian bike plant; CCM no longer the lone domestic bicycle manufacturer. Another company, Sekine, is also planning to build a bicycle plant.

1973/1974
North American bicycle market boom years.

1974
CCM exports expand into Britain, Nigeria, Jamaica, and Australia.

1974
Serious financial losses begin.

1 April 1976
Ben Virgilio joins CCM as executive vice-president and general manager with mandate to turn the company around.

Spring 1977
$6 million fire in St. Jean plant destroyed winter inventory and resulted in major borrowing.

Spring 1977
Indefinite layoff of 200 bicycle-plant employees.

June 1977
Federal government involvement to avert CIBC calling $6 to $8 million in loans to CCM.

June-August 1977
250 employees laid off temporarily.

September 1977
Montreal Gazette states that CCM reported a $1.54 million loss on $67.4 million in sales for the year ended September 1977 (no annual reports available to verify these figures).

November 1977
Anti-dumping Tribunal ruling: introduction of a 'fair market surcharge' on bicycles imported from Taiwan and South Korea to replace a temporary $15 surcharge.

3 March 1978
Globe and Mail states that CCM got $8.2 million in loan guarantees from the EDB to implement restructuring plans. In return, EDB received an option to buy CCM.

March 1978
After five or six years of CCM losses, parent firm Levy Industries, and the ITC and EDB, put CCM up for sale; CCM has $35 million in assets. ITC and EDB keep CIBC at bay for eight months to save plant from closing; CCM given $11 million in loan guarantees and Royal Bank became the firm's main lender.

15 March 1978
Announcement that Maxwell Cummings will buy CCM.

31 May 1978
Announcement that only the drafting of legal documents stand in the way of takeover; three months of negotiations expected to end in two weeks.

29 June 1978
Signing of deal announced; Sheldon Hamer becomes CCM president.

10 July 1978
Montreal Gazette reports that the EDB exercised its option to buy CCM and then arranged Cummings purchase; financial arrangement includes government loans to cover the cost of plant and equipment and financing from the Royal Bank to cover inventory and accounts receivable.

July 1978
Investment of several hundred thousand dollars in retooling for twenty new bicycle models.

Summer 1978
Two new Canadian bicycle manufacturers: Beekay Corp. and Pro Cycle.

August 1978
New duty-valuation regulations for bikes from Poland, Hungary, and Czechoslovakia cause a 50 per cent drop in Canadian imports from these countries.

22 August 1978
Formal announcement of purchase by Cummings with the help of Greenshields Inc.

September 1980
CCM reported a profit of $1.17 million on $58 million in sales for the year ended September 1980.

September 1981
CCM reported a loss of $1.8 million on $61 million in sales for the year ended September 1981.

Early 1982
Bank of New England calls $4 million line of credit; CCM is able to increase borrowing at the Royal Bank only with personal guarantees from owners.

Early 1982
Financing for CCM's proposal to purchase Raleigh Industries falls through; CCM starts negotiating for $10 million in new equity.

May 1982
CCM seeks concessions, UAW Local 28 goes on strike.

30 July 1982
190 CCM Toronto workers have been on strike for eleven weeks.

10 August 1982
Twelve-week strike ends; settlement is 'expensive', making it difficult to attract new investors.

September 1982
CCM reported a loss of $4.3 million on 60 million in sales; lays off some employees.

14 October 1982
CCM asks its creditors for a moratorium on its debt until 31 January.

November 1982
CCM tried to obtain $10 million of new equity, mostly from Maxwell Cummings and to convert EDB loan guarantees into preferred shares; Richter and Partners determined that there would not be enough money to cover the large bank loans.

22 December 1982
CCM accepted offer for purchase of assets of both divisions, transactions expected to be completed in mid-January; proceeds are insufficient to cover amounts owed to secured creditors.

24 January 1983
The Ontario Supreme Court places CCM in bankruptcy.

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10
Electrohome Limited

BACKGROUND

Dominion Electrohome Industries Ltd. was incorporated in Kitchener, Ontario on 1 April 1933. It was an outgrowth of a business established there in 1907 by Arthur B. Pollock to manufacture Phonola phonographs and related equipment. In 1967 the company name became Electrohome Limited. Electrohome is involved in industrial electronics, consumer-electronics production and services, communications, and furniture.

In 1933 Electrohome acquired a Kitchener subsidiary to manufacture radio sets, and in 1936 a woodworking plant was purchased in Kitchener to replace and expand the existing facilities in Elmira. During the war Electrohome was engaged almost entirely in defence work. Normal production did not resume until late 1945. In 1950 the company prospered. The early 1970s were particularly prosperous as Canadians purchased television sets[1] and home-entertainment products in increasing numbers. By the late 1960s and early 1970s Electrohome was facing intense competition as the market became swamped with cheap black and white televisions, radios, and stereos from the Far East, particularly Japan. In 1970-71, in response to the situation, the Electronics Industry Association (EIA) initiated an anti-dumping charge against Far Eastern and American producers. The Association won the decision although it was later overturned on a legal technicality. In 1973-74 the Association initiated a second charge. This time the court determined that dumping had occurred, but that there had been no injury to Canadian producers.

In 1975 Electrohome experienced its first operating deficit since 1952. At this time the company hired Booz Allen, a US consulting firm, to study

its operations. Despite subsequent efforts at re-organization, losses continued until 1977 when the company was assisted by a loan guarantee of $15 million through the Enterprise Development Program administered by the federal Department of Industry, Trade and Commerce (ITC). In late 1978 there was a measure of recovery for Electrohome. The company had continued to restructure its operations, changed its orientation away from the cyclical consumer market, and broadened its product lines. In the 1980s the company has continued to strengthen its market position; recently (1982-83), the company again has experienced financial difficulties (for selected financial information see Appendix I0I). In 1983 this led to a loan from the Ontario Development Corporation (ODC) which is interest-free until July 1984 and repayable over sixty months.

1974-77

Electrohome challenged

In the fiscal year 1974, Electrohome experienced its lowest profit level since 1954. Japanese imports of consumer electronics had peaked,[2] and Electrohome faced intense competition. Competition from the United States in furniture production also intensified. From 1975-77 Electrohome's stock price collapsed, and the company experienced a working-capital deficit in 1975. In part, the problems were caused by the recession – Electrohome was caught in a down-market for consumer durables at a time of company expansion.

Electrohome had received a loan of $1,454,000 (now paid off) from the Department of Regional Economic Expansion (DREE) in 1974 to establish a furniture plant in Stellarton, Nova Scotia.[3] In mid-1977 the plant was closed down at a loss of $3 million; it had never been profitable due to declining demand in the recessionary period. In 1974 Electrohome also incorporated Electrohome (Malaysia) Sdn. Bhd., a wholly owned subsidiary, to construct and generate an electronic sub-assembly plant in Malaysia.[4] This was an effort to benefit from lower labour costs and thereby become more competitive with Electrohome's Far Eastern competitors. However, in late 1977 Electrohome (Malaysia) Sdn. Bhd. ceased production and the assets were subsequently sold.

In 1976 Electrohome entered into a co-operative venture with Advent Corp. of Cambridge, Mass. to develop a giant television screen. Electrohome manufactured chassis for the North American and export markets for Advent. In Canada the product was marketed as an

Electrohome-Advent TV; elsewhere it was marketed under the Advent name alone. Optimistic forecasts predicted that this product could capture a significant portion of the television market. However, consumer spending on durables had fallen and the concept did not excite much interest. Electrohome continued to manufacture the product, but at much lower levels of production than initially anticipated. In the late 1970s Advent Corp. failed and the venture collapsed.

In February 1977 the Royal Bank decided to call its $10 million in short-term loans (payable 31 December 1978) to Electrohome following the company's 1976 operating loss, working capital deficit, and low share prices.[5] The Royal Bank had found that it lacked adequate security for its loans to Electrohome. The bank wanted to secure the loans with a right to call on the assets of Central Ontario TV Ltd., a wholly owned subsidiary of Electrohome. Following negotiations among the Royal Bank, the federal government (EDB), and Electrohome, the bank instead agreed with Electrohome's directors to appoint James Holmes as CEO and Chairman. Holmes's mandate was to install a new management structure with improved communications and financial controls, to improve the working capital and debt positions, and to focus the company towards areas of distinctive expertise. An outsider brought in by the banks and the government, Holmes was not popular but the move forestalled receivership. John Pollock, president of Electrohome, agreed that present management was 'too close' to the situation to have the required objectivity.

The re-organized management moved to rationalize Electrohome by disposing of a number of major assets – the Nova Scotia plant, which the company had been attempting to sell prior to the management change; Flexsteel Industries Ltd., a large upholstery manufacturer whose sales jurisdiction had caused problems; and in 1978, Hawkesville Lumber Ltd. and Electrohome Appliances Ltd. In mid-1977, 650 employees were laid off, lowering the employment level to 2,000. In 1974 employment had peaked at 3,900.[6] However, employment had been stable at approximately 2,200 since that peak. Electrohome completed negotiations, ongoing since 1975, to purchase television components from JVC of Japan; this was desirable because Electrohome's low volume did not make domestic production viable.

In early 1977 Electrohome also benefited from an ITC package, initiated in response to lobbying by then-minister Jean Chrétien, to restructure the television industry.[7] The policy was initiated in response

to the American and Japanese domination of the television market. In all probability it was also linked to the EIA's loss at the two anti-dumping trials – a situation which precluded legal action against Far Eastern and American producers; a policy was thought necessary to enhance the competitive position of Canadian producers. The ITC package gave manufacturers a duty remission on a certain number of imported televisions in proportion to the number built in Canada. A 15 per cent tariff on colour sets imported by other than a Canadian manufacturer would continue through 1981, and the Commonwealth preferential tariff was withdrawn. At this point imports accounted for almost all the black and white television sets sold in Canada and 45 per cent of colour sets.

However, Electrohome also faced problems with declining demand in the furniture-production sector, and overall losses continued through 1977. In earlier periods of difficulty the company's interdependent divisions had been able to support one another. In response to severe financial troubles, Electrohome approached the Enterprise Development Board for a loan guarantee in June 1977.

The loan guarantee agreement

By December 1977 talks with the Enterprise Development Board and the Royal Bank, Electrohome's major creditor, produced a fifteen-year financing package of $25 million, of which $15 million was 90 per cent insured by the EDB.[8] The Royal Bank restructured $10 million of Electrohome's short-term debt, which had been payable on 31 December 1978, into a fifteen-year term. This was secured by a mortgage on Electrohome's real property and additional floating charges. The accounts receivable, inventories, and shares of Central Ontario TV Ltd., a wholly owned subsidiary of Electrohome, were pledged as collateral. The EDB was to collect an annual fee of 1 per cent of any outstanding loans to Electrohome; the loans were insured by the EDB. This package restored Electrohome's working capital to a ratio of 2 to 1, i.e., current assets were twice the level of current liabilities.

The EDB was granted an option on 436,005 class A treasury shares at $2.06 per share until 31 December 1992 or until three years after repayment of the loan;[9] 996,584 of 1,245,730 shares belonging to J. Pollock and the estate of C.A. Pollock were pledged to the Royal Bank. These represented 33 per cent of Electrohome's outstanding shares.

Electrohome also received indirect assistance from Ottawa. In October 1977, the Department of Supply and Services awarded a $282,000 contract to Electrohome for research and development in solar energy.[10] In September 1978 the Ontario Ministry of Housing – the Ontario Housing Corp. project – awarded Electrohome a $60,000 contract for its solar-heating system which had been designed at the University of Waterloo.[11]

1978-1983

Recovery and continued re-organization

Electrohome began to recover in 1978. Its financial situation was extremely complex – it included stock options, co-insured loans, and share pledges – with the Royal Bank, the EDB, and the Pollock family and Holmes' management team as major participants. However, Electrohome now had the long-term capital and financial security necessary to re-organize. Holmes claimed a 'cautious optimism' concerning the company, noting that its backbone – the furniture and consumer-electronics divisions – remained troubled.[12] The television market was soft and the formerly reliable line of Deilcraft furniture was not selling well.

Commencing in 1978 Electrohome broadened its service and communications divisions, and worked to increase revenues from industrial products. Aabex Ltd., Electrohome's servicing division, was created from Electrohome's consumer and industrial products divisions. Aabex has the capability of dealing with more sophisticated computer systems and performing other high-technology maintenance work. In 1981 Electrohome ventured into satellite communications with Gensat Communications Corp. and in 1980 it became the sole supplier of equipment to the government's Telidon two-way TV systems. The company restructured to take better advantage of its technical expertise by applying it to the production of industrial and communications products for which demand was growing and profit margins were higher. Reliance on cyclical consumer products was reduced. In future, the company would not attempt to compete with the Japanese in the consumer-electronics business.

In 1972 consumer products had represented 80 per cent of revenue,[13] by 1980 the figure was 45 per cent,[14] and by 1981, 35 per cent.[15] Service and communications revenue increased from 2 per cent of sales in 1976 to 18 per cent in 1979. Industrial revenue rose from less than 20 per cent of

sales in 1976 to 33 per cent in 1979, and to 48 per cent in 1980.[16] The goal for 1985 was that video-game components, video display terminals and industrial products would represent 60 per cent of sales.

Electrohome also continued to reduce its dependence on the domestic market. The Canadian market was considered too small for high-cost consumer goods. Electrohome moved into high-technology 'custom-engineered, batch manufactured products,'[17] which it exported. The depreciation of the Canadian dollar contributed a great deal to the company's competitive position in 1980, while the boom in arcade games and micro-computers provided a good market for both electronic component products and service. By 1980 video screens provided 33 per cent of company revenue, twice the 1978 contribution. They also account for most of the seven-fold increase in Electrohome's exports since 1975.[18]

Electrohome reduced its long-term debt from $31 million in 1977 to $3 million in 1980. This reduced the effect of record-high interest rates. The percentage of debt to total capitalization dropped to 70.7 per cent in 1979 from 83.5 per cent in 1977, with the company aiming for a level of 35 per cent by 1985.[19] Electrohome managed to double sales from 1977-1980 while assets increased by only 22 per cent.[20] This provided an increased cash flow, and permitted Electrohome to pay off its debt to the EDB by December 1980.

Electrohome's share prices reflected the improvements in its market position. In 1978-79 stock had traded in the range of $2 to $6; in 1980 prices reached a high of $17.50; and in 1981, $26.25 (see Table 22). In June 1981 Ottawa sold the Electrohome shares it had purchased at $2.06 per share as part of the loan-guarantee agreement for approximately $30.25 per share. The EDB earned $10 million from this sale of Electrohome stock.[21]

James Holmes resigned in the summer of 1980, to be replaced by Stewart MacLellan as CEO. John Pollock assumed the chairmanship. Holmes considered that he had completed his task by helping to restore Electrohome to a competitive position. Certainly, Electrohome now enjoyed a larger volume of business and more diversified activities than it had in 1977 but its furniture division was still in some difficulty. Electrohome had experienced a decade of uncertainty in sales, earnings, and stock prices.[22]

TABLE 22

Electrohome Limited: Historical summary (as originally stated in company's annual reports for the respective years)

Fiscal year	Total assets	Fixed assets	Working capital	Shldrs.' equity	Debt[a]	Sales	Net inc. oper.	Earns. per sh.[b]	Price range High	Price range Low
	($000s)							$	$	$
1974	75,204	18,977	11,857	22,192	39,100	107,057	147	0.02	9.25	4.00
1975	63,984	19,271	5,792	18,597	33,200	87,545	d3,481	d1.20	6.88	3.40
1976	65,799	18,221	d2,027	10,491	39,700	93,660	d5,116	d1.74	5.63	2.45
1977	57,766	15,146	20,158	7,385	37,400	92,147	d3,087	d1.06	3.90	1.72
1978	53,445	12,591	20,277	8,126	33,600	98,224	692	0.20	5.13	2.05
1979	67,158	13,251	23,934	12,864	31,000	128,695	3,369	1.09	6.13	3.75
1980	70,300	14,763	23,974	28,628	21,200	183,985	9,546	3.07	17.50	4.25
1981	100,988	17,917	30,666	38,273	29,600	232,181	8,475	1.64[c]	26.25[c]	7.75
1982	82,409	20,940	21,549	35,928	28,000	162,520	d1,090	d0.21	12.00	4.00
1983	71,269	22,232	22,533	32,346	23,300	142,121	d3,298	d0.62	9.25	3.90

a Long- and short-term.

b Common shares reclassified as class A and B shares from 25 April 1974 to 30 May 1980; reclassified as common shares to 19 June 1981; and reclassified as class X and Y shares thereafter. Price range for class X shares are shown.

c Following 3-for-1 split in 1959; a 5-for-1 split in 1972; and an effective 3-for-2 split in 1981.

SOURCE: Electrohome Limited Annual Reports 1974-83.

Electrohome Ltd. remains in a state of transition. In early 1983 the company concluded an agreement with Mitsubishi Electric Corp. of Japan to produce several thousand television sets a year with parts to be supplied by Mitsubishi. In the high-technology sector it has a joint venture in Gensat Communications Corp. that provides entry into the private satellite television earth terminal receiver and accessory business on an international basis. Its involvement with Telidon has not paid off yet. However, the company did not expect the venture to contribute to profits until 1984.

Electrohome has left the air-conditioner, humidifier, and dehumidifier business completely, other than maintaining the Electrohome trade name. The company now focuses on electronics and motors, furniture and electronic product services, and TV and radio broadcasting. It has been successful in shifting away from the consumer sector as industrial products accounted for 60 per cent of revenues in 1983. The consumer TV business was sold to Mitsubishi of Japan. However, models continue tobe made at the Electrohome plant in Kitchener under an arrangement with Mitsubishi. 'The impact of restructuring operations, market weakness in certain product areas, and a generally soft economy'[23] contributed to a 1982 net loss of $1.1 million on $162.5 million in sales, a trend which continued with 1983 losses of $3.3 million on $142.1 million in sales.[24] In the first nine months of 1984 (ended 28 September) Electrohome's net loss was $2.4 million on sales of $95.2 million, down 9 per cent from the same period in 1983.[25] Electrohome's most profitable business is its television station, CKCO-TV in Kitchener, which is an independent operation. Electrohome has continued a high rate of capital expenditure on research and development as the company proceeds in its transition from a consumer product manufacturer into a producer of high-technology commercial and industrial equipment.

FINANCIAL TREND ANALYSIS

To observe the financial health of Electrohome leading up to and emerging from the bailout in 1977, some financial ratios will be calculated and analysed. The period of analysis is 1974 to 1979, thereby providing information on the structure of the firm as it emerged from the bailout.

The financial ratios considered are presented in Table 23. Prior to the bailout – 1974 to 1976 – it is clear that the company had serious financial problems. The liquidity ratios (1 and 2) demonstrate a lack of current

TABLE 23
Financial ratios: Electrohome Limited

	1979	1978	1977	1976	1975	1974
1 Current ratio[a]	1.85	2.09	1.99	.96	1.16	1.28
2 Quick ratio[b]	.84	1.02	.79	.30	.45	.45
3 EBIT[c]/(interest + preferred div./.5)	2.35	1.41	.36	(.21)	(.57)	1.44
4 EBIT/Average total assets	.18	.10	.02	(.01)	(.03)	.02
5 Net income/sales	.04	.01	(.03)	(.09)	(.04)	.001
6 Sales/Average total assets	2.13	1.77	1.49	1.44	1.26	1.59
7 5x6: Return on assets	.08	.01	(.05)	(.12)	(.05)	.002
8 Debt/(common + preferred)	1.80	3.01	3.96	.71	.45	.41
9 (Debt + preferred)/ common equity	2.17	3.90	5.21	.99	.58	.52
10 Z	.95	.77	.18	(1.66)	(.64)	(.19)

a Current ratio ≡ current assets/current liabilities.
b Quick ratio ≡ (current assets – inventories)/current liabilities.
c EBIT ≡ earnings before interest and taxes.
SOURCE: Financial Post Corporate Service

assets to cover the current liabilities, a problem which led the Royal Bank to call its loan early in 1977. The coverage ratio (3), which captures the ability of the company to cover its fixed financial commitments out of earnings, was deteriorating in 1975, was negative in 1976, and improved in 1977 at the time of the bailout. The poor coverage ratios reflect both poor profitability (ratio 4) and an increasing ratio of debt to equity (ratio 8 or 9). The return on assets (ratio 7) defined as the ratio of net income to total assets, is very low or negative. The components of this ratio are found in ratios 5 and 6. Ratio 5 measures the profitability generated from sales (i.e., reflects the importance of both operating and financial expenses); ratio 6 reflects the turnover of assets to generate sales – a measure of the efficient use of assets. For Electrohome the low return on assets is primarily caused by poor profitability (5), but the turnover ratio also deteriorates, and then improves marginally in the year of the bailout. The final financial ratio is the Z score, ratio 10, which provides a measure of the probability of bankruptcy.[26] The value of Z is obtained by inserting a set of ratios into an equation; the ratios and the equation have been identified by using financial information for a set of bankrupt and nonbankrupt companies over a sample period.

When the value of Z is negative, the firm is classified as bankrupt. Based on Electrohome's operations in 1974 through 1976, the company was classified as bankrupt.

Subsequent to the bailout there was an improvement in many of the financial ratios. The current ratio improved as short-term was converted to long-term debt. The quick ratio also improved, but in 1979 began to show signs of deterioration. With the improvement in earnings (see 4) came improved coverages (3). The improvement in the return on assets ratio (7) arose from improved profits (5) and a substantial increase in turnover (6). Instead of raising equity the company issued more debt and this increased the debt ratios (8 and 9). The company subsequently paid off debt, reducing its leverage. Finally, the Z values are positive, indicating the end of financial distress.

In sum, the bailout was structured to improve working capital and coverages of the firm and to permit it to compete. The subsequent profitability of the company appears to be a result of improved efficiency in its operations and strategic marketing decisions.

NOTES

1 *Financial Times Canada* 30 May 1977. In 1972, 70 per cent of sales were colour televisions for consumers.
2 *Canadian Business* July 1978.
3 *Executive* October 1980
4 *Financial Post Corporation Service* 10 August 1982.
5 *Financial Post* 26 February 1983.
6 *Financial Times Canada* 30 May 1977.
7 *Financial Post* 29 January 1977.
8 *Toronto Star* 31 December 1977.
9 *Financial Times Canada* 1978.
10 Toronto *Star* 30 October 1977.
11 *Globe and Mail* 4 September 1978.
12 *Financial Times* 13 November 1978.
13 *Canadian Business* July 1978.
14 *Globe and Mail* 31 May 1980.
15 *Financial Times* 1 June 1981.
16 *Ibid.*
17 *Ibid.*
18 *Financial Times* 16 June 1980.

19 *Financial Post* 27 September 1980.
20 *Financial Times* 1 June 1981.
21 *Globe and Mail* 13 June 1981.
22 *Financial Times* 30 January 1984.
23 *Financial Times* 30 May 1983.
24 *The Financial Post Corporation Service* 15 November 1984.
25 *Financial Post* 24 November 1984.
26 E.I. Altman and M.Y. Lovalee (1980) 'Business failure classification in Canada'. *Journal of Business Administration* (Fall) 147-64.

11
Consolidated Computer Inc.

BACKGROUND

Consolidated Computer Inc. (CCI) was founded by Mers Kutt in Ontario in 1968. During the 1970s it was one of the largest Canadian-owned and controlled computer-hardware manufacturing companies with average sales of $1.5 million. CCI specialized in data entry systems and small business terminals.

CCI entered the market with products that were revolutionary for their time. However, it suffered from inadequate financing and limited marketing ability; the capital required to lease its products exceeded the company's resources. The startup costs in a sector characterized by rapid growth, constant technological evolution, and intense international competition were extremely large and CCI never knew financial stability (see Table 24).

In June 1969 CCI went public, raising $8.4 million through an issue of 412,000 shares and $5.5 million in convertible debentures.[1] By mid-1970 these funds were exhausted. By 1971 the Ontario and federal governments were supporting CCI through industrial-assistance programs. CCI entered receivership in November 1971, and was bailed out when Ottawa (through the General Adjustment Assistance Board) and Ontario (through the Ontario Development Corporation) paid out $8.8 million of CCI's bank indebtedness in exchange for $4.4 million of debentures and an equity position. From 1972 to 1976 Ottawa and Ontario extended $16.6 million in further loan guarantees to the company. In 1976 Ottawa unsuccessfully attempted to arrange the sale of CCI to Central Dynamics Ltd. When this deal fell through, the two governments took steps to re-

TABLE 24

CCI: Selected financial statistics

(In $000)	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982 [a]	1983 [b]
Current assets (CA)	4738	7066	13662	12898	15544	14610	21929	13004	8952	12267	8866	5687
Total assets (TA)	7362	10035	21708	25107	20393	16485	22878	13794	12872	14490	11657	9642
Current liabilites (CI)	1897	5348	22202	39614	13206	11905	19623	16303	25914	12211	10258	24033
Long-term debt (LTD)	8384	9390	6967	3821	5954	5699	4445	8175	11119	49343	50544	51122
LTD + current portion	9449	9490	9411	9042	6208	5954	5699	8429	11360	49412	51109	51191
Equity	(2912)	(5191)	(10687)	(23563)	(2211)	(1803)	(1189)	(10686)	(24161)	(47064)	(49993)	(64935)
Year-end working capital (WC)	2842	1718	(8539)	(26716)	2338	2705	2306	(6044) [c]	(16962)	56	(1662) [d]	(18346) [d]
Change in WC	942	(1124)	(10257)	(18766)	29054	367	(399)	(8350) [c]	(10919)	17019	(1718)	(16684)
Net sales	11955	12056	15395	15809	25299	18812	23047	22698	11924	17291	11210	24142
Gross margin	5374	2371	1569	(98)	9758	7751	10510	3363	(1333)	(4583)	N/A	N/A
Net income	2002	(2571)	(5496)	(12876)	24	418	614	(9997)	(13475)	(22903)	(2929)	(5444)
Net income per share (before extraordinary items)	.28	(.67)	(1.43)	(3.34)	(almost nil)	.02	.03	(.53)	N/A	N/A	(.16)	(.29)
CA/CL	2.50	1.32	.62	.33	1.18	1.23	1.12	.80	.35	1.01	.86	.23
Sales/total assets (TA)	1.62	1.20	.71	.63	1.24	1.14	1.01	1.65	.93	1.19	.96	2.50
Gross margin/sales	.45	.20	.10	(.01)	.39	.41	.46	.15	(.11)	(.27)	N/A	N/A
Net income/sales	.17	(.21)	(.36)	(.81)	nil	.02	.03	(.44)	(1.13)	(1.32)	(.26)	(.23)
LTD/TA	1.14	.94	.32	.15	.29	.35	.19	.59	.86	3.41	4.34	5.30
LTD + current portion/TA	1.28	.95	.43	.36	.30	.36	.25	.61	.88	3.41	4.38	5.31

a for the six months ended 2 July 1982 – vs. previous reporting periods end 31 December

b for the twelve months ended 2 July 1983 – vs. previous reporting periods end 31 December

c figures as restated in 1980 annual report

d figures derived from change in WC over the year. Year-end WC not reported.

SOURCE: CCI Annual Reports 1973-83.

structure CCI. By the end of 1976 Ottawa and Queen's Park controlled 65 per cent of CCI's stock. CCI earned modest profits in 1977 and 1978. However, heavy losses were incurred again in 1979, 1980, and 1981, and the governments were compelled to pay off $42 million in insured bank loans to CCI. In March 1982 CCI was sold to Nabu Manufacturing Corp., an Ottawa-based computer company. Ottawa had lost a total of $116 million and Ontario about $9 million in their decade of support for CCI.

One of the company's problems was the failure of CCI to recognize and take action to deal with rapid changes in the commercial, financial, and market environments in which it operated. CCI continued to manufacture its Key Edit data-entry system long after more efficient systems were developed. This system takes data from a large computer in the form of keyed information on a terminal, puts it on a disc following verification, then transfers it to a tape. It became obsolete in the mid-1970's with the development of 'intelligent terminals' which could more efficiently perform this process within the large terminal.

Some strength came from CCI's export capacity, particularly its contracts with International Computers Ltd. (ICL) of Britain, Ecodata of Brazil (a subsidiary of Cable and Wireless Ltd.), and Fujitsu of Japan. CCI and Fujitsu signed a technology-assistance agreement in July 1976 to share the cost of computer product development, and to provide Fujitsu with a toe-hold in the North Amercian market. This deal was one of CCI's only hopes for recovery and stability in the late 1970s.

1968-1974

Receivership and re-organization

Consolidated Computer Inc. entered the computer market in the peripheral area (feeding the main computer and allowing it to work more effectively) since this was a market in which it was possible to compete with the giant corporations in the field. CCI's Key Edit system was designed to speed up data preparation, correct it, get it into a small central processing computer, store it, transfer it to magnetic tape and then have it ready to flow into the main computer.[2] This process was more efficient than conventional methods, cards, and card readers, and thus reduced costs.

By late 1971, CCI had a backlog of $10 million in orders.[3] The nature of the business of leasing computer hardware precipitated a series of liquidity crises. IBM, as the major force in the market, had adopted the

practice of leasing computer equipment, a practice which competitive pressures forced new firms to follow and which affected short-run profitability. CCI was required to pay immediately for manufacturing and marketing its machines, but was paid back only gradually through rentals. CCI had to gamble on a long- term payback beyond the fifty-month lease-buy crossover point; it cost $100,000 to make, market, and service one of its machines, but the customer paid only $30,000 per year to lease.[4] Its working-capital requirements were therefore large, and leasing did not generate the necessary short-term revenue to finance the manufacture and marketing of more units. By 1970 this situation had led to the exhaustion of funds generated through the 1969 sale of shares and convertible debentures.

The problem was alleviated in the short term with federal assistance provided by the General Adjustment Assistance Board (GAAB) under a program administered by the Department of Industry, Trade and Commerce (ITC). In early 1971 GAAB agreed to provide $12 million in loan insurance for CCI's leasing operations, in addition to the $1.3 million in R&D grants CCI had already received under the Program for the Advancement of Industrial Technology (PAIT) and the Industrial Research and Development Incentives Act (IRDIA).[5]

The Ford Motor Credit Co. agreed to provide loans to CCI, and the two companies established a leasing company called Consolidated Computer Leasing Corp.[6] CCI would sell the lease contract for its Key machines to CCL Corp., in return for the full purchase value of the machine. CCI would then lease the machine from the lease company for renewable one-year periods on behalf of its customer. Thus, CCI would gain less residual revenue from machines financed through Ford than from those internally financed, although it received immediately the capital necessary to finance current production and expansion. CCI could take into its accounts profits on the sale of its Key Edit equipment and still retain substantial equity in both the financing profits and the residual value of the equipment.[7] However, in June 1971 CCI agreed to use more conservative accounting methods so its current revenue statements would be less inflated.

By late 1971 CCI was once again experiencing a severe liquidity crisis. On 4 September 1971 the Ontario Securities Commission suspended trading at CCI's request.[8] CCI owed $13 million to creditors, $9 million of which was unsecured. On 13 November 1981 CCI entered voluntary receivership.

The rescue of CCI

Debate on whether to keep CCI afloat centred on its value as a promising Canadian computer company – a symbol of Canada's technological capacity. Members of the federal Liberal government argued that Canada must develop computer companies or Canadians would not enjoy a share of the high-skill and high-education jobs that the industry offers. Other national governments, such as Germany, were supporting and creating computer industries. A press report noted that the $1.3 million advanced to CCI in research and development grants was less than one-tenth that given in 1970 to IBM Canada Ltd. and Control Data Canada Ltd., both wholly owned subsidiaries of US companies.[9]

In December 1971 a number of proposals to re-organize CCI were put forward by the company. Re-organization arrangements were put in place in 1972 after CCI defaulted on its 1970 loans from the Ford Motor Credit Co.[10] CCI's co-founders, president Mers Kutt and vice president Donald Parmenter, signed a $20-million, two-year (February 1973 to July 1975) sales contract with International Computers Ltd. (IDC). It was intended that ICL provide a solid sales base and cash-flow backing for growth.[11] The contract ensured a minimum production base of ten systems per month. CCI's creditors accepted convertible debentures and shares in settlement of their claims. They could recover 100 percent of their claims on CCI if and when CCI stock reached $3.50 per share.[12] Chief among these creditors was Digital Equipment of Canada Ltd. whose trade with CCI was worth over $1 million per year.[13] Ottawa (GAAB) and Ontario (ODC) provided new financing and paid insurance claims on existing loans amounting to $8.8 million in return for $4.4 million of debentures and 40 per cent of CCI's equity (51 per cent of voting stock).[14] As part of the agreement, Donald Early was named chairman of CCI.

1972-1974 were years of optimism for CCI with new products and deals with ICL and Fujitsu. The federal government continued to provide loan insurance with which CCI built a North American branch network, leased a new plant, and maintained strong research and development funding.[15] However, CCI's net income continued to decline (Table 24).

1975-82

Re-organization and negotiations for sale

1975 was a very difficult year for CCI; sales did not increase significantly and a loss of $13 million was incurred on sales of $16 million. Employment fell from 675 to 450 in one year. In December 1976 financial re-organization increased outstanding common shares to enable the two governments to convert $21 million of their various debt instruments into common stock. Since 1970 Ottawa and Queen's Park had contributed more than $25 million in loans, grants and loan insurance.[16]

Negotiations continued throughout 1976 for a loan of $30 million from private-sector sources to CCI's leasing vehicle (Financeco and Finecomp) to finance leasing sales – the GAAB had agreed to insure 99 percent of the loan.[17] In 1977 the Enterprise Development Board, the successor to GAAB, agreed to insure a further $30 million in lease financing. However, CCI continued to suffer from a chronic lack of capital.

In December 1976 Ottawa held 53 percent of CCI, the Ontario Development Corporation held 16 percent, Fujitsu held 23 percent, and the public held 8 percent.[18] Ottawa and Queen's Park both wished to reduce their combined position to that of minority shareholders. In January 1976 Ottawa attempted to negotiate the sale of CCI to Central Dynamics Ltd., a company involved in the production of specialized television broadcasting equipment and the provision of computer terminals. During the negotiations a management team from Central Dynamics was installed at CCI. The team included Earle Wallick who became chairman of CCI and Leslie Sellmeyer who became president (Sellmeyer retained his position until mid-1980 when he was replaced by government-appointed John Brown). In October 1976 Central Dynamics withdrew from the proposed purchase arrangements with CCI and the governments due to the 'growing complexity of the deal.' The Treasury Board had repeatedly stalled on its final approval of the sale arrangements because Central Dynamics had wanted greater control for its management team to restructure CCI and to improve its efficiency during the negotiation period. However, the government had insisted on keeping Central Dynamics at arm's length until the sale was finalized.[19]

In July 1976 a technology-assistance agreement was signed with Fujitsu of Japan for which Fujitsu received 700,000 of CCI's shares in exchange for technology. CCI and Fujitsu were to co-operate in the Inagi I and II computer projects. Another $3 million in shares plus options on a

further 5 per cent was granted to Fujitsu in return for Fujitsu's commitment to provide technical, manufacturing, financial, and marketing assistance.[20] CCI would receive the manufacturing and distribution rights to Fujitsu products in North America. CCI thus became a vehicle to market Fujitsu products in North America, and acquired the capacity to develop new products.

Following the Fujitsu deal Ottawa believed that CCI could stand on its own without further financial backing. The EDB had inserted new management and some of its own directors. From 1976-78 CCI actually did register small profits, but interest rates were taking their toll, and in 1979 CCI began to show losses despite relatively strong sales (compared to average sales over the past five years). In 1978 CCI defaulted on a $6 million short-term loan designed to enable the company to undertake major contracts for the provision of lottery terminals in Ontario and Quebec.[21]

By April 1978 the estimated book value of the Crown's shares was negative $906,149, and no profit had been realized on a total federal investment of $19,430,000.[22] Ontario held a 16 per cent interest consisting of 2.8 million shares in CCI and guarantees, and a line of credit to finance export activities provided by the ODC amounting to $5.6 million. The rationale behind this investment was to recognize the 'considerable contribution of the company in developing and marketing abroad Canadian technological expertise, as well as [CCI's] important present and future employment significance.'[23]

However, after a loss of $10 million in 1979, the Ontario and federal governments began to re-assess CCI's long-term viability. Heavy spending and financing costs incurred through the heavy capital demands of leasing were a major cause of CCI's continued losses. In June 1980 the federal government inserted a new management team headed by J.M. Brown. In spite of this, in 1980 CCI lost $13.5 million on sales of only $11.9 million, causing the governments to seek a termination of their involvement with the company. In June 1981, Herb Gray, then minister of industry, trade and commerce, stated that Canada needed a healthy CCI that could counter Canada's $1.26 billion trade deficit in computers and office products. He stated that CCI could turn around with a three-year business plan that included cost-cutting, sales stimulation, and subcontracting negotiated with other 'original equipment manufacturer' (OEM) customers.[24] On 25 June 1981 an ITC press release announced that the government would refinance those loans carried by CCI and its

leasing affiliates that were insured by the EDB. CCI interest payments were running at about $1 million per month.[25] The government pledged to absorb all outstanding debt to enable CCI to carry out the business plan developed by the interim management installed in mid-1980, which included two ITC officials. The release noted that CCI had experienced problems adjusting to rapid technological changes and developing effective marketing strategies. The sale of Crown-owned shares in CCI by 31 December 1981 was deemed the most cost-effective solution.

Return of CCI to the private sector

In November 1981 Gray announced that the federal and Ontario governments were selling their combined 64 per cent of CCI's equity to Nabu Manufacturing Corp.[26] Public and Fujitsu shareholdings were not involved.

Nabu Manufacturing Corp. is an Ottawa-based producer of television converters and microcomputers that was formed on July 1, 1981 from a merger of six smaller firms and the subsequent private placement of $18.5 million in shares among investors, including Michael Cowpland, co-funder of Mitel Corp. Nabu's chairman, John Kelly, and President Denzil Doyle stated that Nabu was seeking CCI's manufacturing capacity. The service and contract commitments that Nabu would acquire were anticipated to be worth $1 million a month.[27] In addition, CCI had 350 skilled employees in Canada who were an important resource in an industry suffering an acute shortage.

Nabu agreed to pay $1 for the two governments' 12 million shares (at 49 per cent interest), plus $100,000 in cash for CCI debt notes of about $47.4 million outstanding to the federal and Ontario governments.[28] However, it is unlikely that CCI can ever pay the $47.4 million debt to Nabu since it is debt-ridden with a negative equity value. Some $7.5 million is expected to be recovered by the government by the end of 1986 in the form of participating payments based on percentages of lease revenue to be earned by Financeco and Finecomp. Nabu agreed to provide enough working capital to keep the CCI manufacturing operation in production for at least two years and to guarantee Ottawa's receipt of leasing revenues. Nabu agreed to have CCI and its leasing vehicle Financeco waive all claims for income tax loss-carry-forwards with respect to previously accrued losses.[29] Jobs were also to be maintained either within CCI operations or through a transfer to Nabu.

The federal and Ontario governments agreed to pay off all bank loans of CCI, Financeco, and the U.S. leasing subsidiary Finecomp. Government-insured loans outstanding at 30 November 1981 amounted to $91 million ($88 million federal plus $3 million Ontario) including $47.4 million to CCI and $43.6 million to Financeco and Finecomp.[30] By December 1981 Ottawa stated that government losses totalled $125 million.[31] An additional $3 million (totalling $94 million) was authorized by cabinet to provide contingency funds to permit CCI to meet its interest costs and operating short-falls in the weeks before closure of the deal. (Only $92 million was actually disbursed, of which $3 million was recovered from Ontario).

The $125 million government losses ($119 million contributed by Ottawa and $6 million by Ontario) from grants and coverage of insured loans to CCI and its leasing affiliates are the largest generated in the history of the Enterprise Development Board.[32] (The EDB had taken over responsibility for CCI from the GAAB when the ITC program was changed in 1977.)

Nabu and CCI were to develop complementary strategies in research and development, future product lines, and marketing. Nabu wished to broaden CCI's relationship with ICL. However, it terminated the technology connection with Fujitsu because it exhibited little interest in continuing with the Inagi II computer-system joint project. Fujitsu had poured several million dollars into the program and expressed concern that the government was discontinuing its involvement with CCI.[33]

In December 1982 it was announced that Nabu Manufacturing, one year after acquiring its 65 per cent interest in CCI, had made a profit of $2.3 million on its investment.[34] In 1983 Nabu split into two companies. Computer Innovations Distribution Inc. was the spin-off which received Nabu's CCI holding. Fujitsu of Japan owns 25 percent of CCI. Since acquiring CCI, Nabu had assumed CCI's debts and invested a further $20 million, although it cut back on CCI's research and development, marketing, and product lines. In March 1984, Computer Innovations placed CCI into receivership because CCI had defaulted on debts of $117 million. CCI is to be managed by its receiver Clarkson Co. Ltd. as a going concern.

THE POLITICAL IMPLICATIONS OF GOVERNMENT ASSISTANCE TO CCI

Douglas Kendall, chairman of the EDB and the GAAB from 1972 to 1982 and a director of CCI from 1976 to 1980, has stated that the decision to

support CCI through the years was made in good faith.[35] It would have been better to discontinue assistance at an earlier time; however, the Canadian government wanted a Canadian computer company and thought the cost of continuing would be less than that of winding down. There is evidence that Ottawa knew as early as mid-1980 that CCI was in serious trouble. The revelation of this evidence has prompted Opposition accusations of mismanagement and a lack of government accountability.

In February 1982 Don Blenkarn MP noted that Donald Johnston, then president of the Treasury Board, had received a letter from ITC dated 23 June 1980 which advised that CCI had lost $10 million on $22 million of sales in 1979.[36] Nearly eleven months later Johnston advised Herb Gray, in a letter dated 12 May 1981, that he was 'not convinced that CCI prospects warrant further government investment.' He also privately warned Gray that 'the government will be severely criticized for its handling of the [CCI] matter, and this criticism will be even greater if the company is further assisted and fails.'[37] In reply to Blenkarn, Johnston stated that in 1981 he hired outside specialists, Bill Rosenfeld, a Toronto lawyer, and Terry Godsall of Shieldings Investments, to determine the viability of CCI. When their findings were available and revealed that proper inventory and financial controls did not exist at CCI,[38] arrangements were made to sell the government equity in the company.

Following the sale to Nabu, Treasury Board commissioned a study into federal dealings with CCI. Written by General William A.B. Anderson, special adviser to Donald Johnston, parts of the report were leaked to Sinclair Stevens, who had been Treasury Board President in 1979 under the Clark government. General Anderson concluded[39] that CCI was never a financially viable company, and a review of its financial statements at any point in its history would have confirmed this. Instead, from 1 January 1980 to 30 November 1981, the government approved seventeen separate loan guarantees worth $30.9 million without a close look at the company's financial situation.[40] General Anderson concluded that government support of CCI from 1971-81 was influenced by significant conflicts of interest, bad advice, and poor information.[41] Except for the first two years (1971-2), CCI was said to have few assets, tangible or otherwise, that would support the investment decisions made.[42] Treasury Board had continually sought to end government support for CCI. However, ITC had been successful in maintaining the company through the Enterprise Development Board. EDB members received no overview on the government's total in-

volvement in the company. Sinclair Stevens termed government dealings a 'web of corporate shell games, apparent deception of ministers by federal civil servants on the CCI board [John G. MacDonald Brown, president of CCI, was inserted by EDB, of which he was a member, and Douglas Kendall, EDB's chairman, also served on the CCI board] and the failure of Cabinet and Parliament to guard the public purse.'[43]

The issue of bureaucratic conflict of interest was a focus of political debate. William Holtzman, spokesman for the Electrical and Electronic Manufacturers Association of Canada, called for an outside investigation into why the bureaucracy continued to give optimistic reports on CCI to the government.[44] Progressive Conservative MP Elmer Mackay noted that John MacDonald Brown, a member of the EDB (although nonvoting on CCI issues) and president and CEO of CCI from June 1980 until the sale to Nabu, had submitted an application on behalf of himself and some associates to purchase the government's shares in CCI.[45] His position as president and CEO would not encourage objectivity in his part as a member of the EDB in consideration of the sale. Sinclair Stevens added that Brown is a noted Nova Scotia Liberal.[46] Mackay furthered the allegations of patronage by noting that Ottawa-appointed officials Gordon Hughes and Green are also prominent Liberals.[47]

In response to allegations such as these the government initiated a study by the Department of Justice to investigate Ottawa's involvement in CCI. A Toronto law firm was asked to review the case within the narrow context of legal culpability. On 8 July 1982 the Department of Justice took the position that there were no grounds for legal proceedings with respect to CCI. The Conservatives responded by demanding a full-scale study by a standing committee of the House on the prevention of future losses of such magnitude.[48] Herb Gray's reply was that the Clark government had done nothing about the situation during its term, and it was the Liberals who had cleaned up the issue.[49]

In addition to allegations of patronage and conflicts of interest, the Conservatives accused Ottawa of acting with impropriety in the financial accounting of CCI. The National Trust Company held one share of CCI's leasing affiliate, Financeco, in trust for St. Michael's Hospital, Mount Sinai Hospital, and the Hospital for Sick Children. Federal MP Don Blenkarn termed this an avoidance of proper disclosure in financial statements since the hospitals were unaware of the arrangement. He questioned why Gray did not look at a consolidated CCI and Financeco balance sheet and why he allowed the use of two separate corporations to

continue when CCI and its leasing affiliate were both actually banked, guaranteed, and managed by the EDB.[50] The government replied that the share was held in trust because it had been agreed on 15 June 1976 that any surplus funds that might have remained after the lease company had paid its bank loans and CCI collection fees were to be given to charitable organizations.[51] On 26 November 1981 the share was redirected to Nabu for $1 cash.[52]

NOTES

1 *Financial Post* 11 September 1971.
2 *Ibid.*, 30 May 1970.
3 *Ibid.*, 11 September 1979.
4 *Ibid.*
5 *Ibid.*
6 The fate of this company was not apparent from press reports.
7 *Financial Post* 11 September 1971.
8 *Ibid.*, 18 December 1971.
9 Ibid., 11 November 1972. The German government was providing $1,200 million for the development of a national computer company.
10 *Financial Post* 18 December 1971.
11 *Ibid.*, 30 September 1972.
12 *Ibid.*, 8 January 1972.
13 *Ibid.*, 18 December 1971.
14 *Toronto Star* 6 December 1981.
15 *Canadian Business* March 1982.
16 *Financial Post* 18 January, 14 February 1975.
17 *Ibid.*, 14 February 1976.
18 *Hansard* 20 December 1979.
19 *Globe and Mail* 14 October, 4 November 1976.
20 *Financial Post* 8 January 1977.
21 *Ibid.*, 27 February 1982.
22 *Hansard* 20 April 1978;
23 *Debates of the Ontario Legislature* 10 June 1980.
24 *Globe and Mail* 13 July 1981.
25 *Financial Post* 27 February 1982.
26 *Globe and Mail* 22 November 1981.
27 *Ibid.*, 14 December 1981.
28 *Ibid.*

29 Ibid., 22 November 1981.
30 *Ibid.*
31 *Hansard* 23 November 1982. Total government loans – $12.9 million with $5 million repaid and the balance converted to common shares; total authorized loan guarantees – $150.7 million with the Crown required to disburse a net amount of $96 million; grants – $10.4 million; no letters of comfort. (Financeco owes the government $20.4 million, while Finecomp owes $8.2 million.)
32 *Toronto Star* 6 December 1981. The EDB can make loan guarantees to a total of $1 billion without special authorization from cabinet or the House of Commons (*Maclean's* 1 March 1982).
33 *Ibid.*
34 *Financial Times* 6 December 1982, 3
35 *Ibid.*
36 *Hansard* 25 February 1982.
37 *Maclean's* op.cit.
38 *Toronto Star* 6 December 1981.
39 *Ibid.*, 20 February 1981.
40 *Financial Post* 27 February 1982.
41 *Toronto Star* 20 February 1981.
42 *Globe and Mail* 20 February 1982.
43 *Maclean's* op.cit.
44 *Globe and Mail* 8 July 1982.
45 *Hansard* 10 May 1982.
46 *Ibid.*, 19 February 1982.
47 *Ibid.*, 10 May 1982.
48 *Ibid.*, 8 July 1982.
49 *Hansard* 23 July 1982.
50 *Ibid.*, 19, 24 February 1982.
51 *Ibid.*, 23 November 1982.
52 *Ibid.*, 19 February 1982.

12
Maislin Industries Ltd.

BACKGROUND

Maislin Industries Ltd. was a Montreal-based, Canadian-owned trucking firm which owned numerous subsidiaries[1] in both Canada and the United States. It was founded in 1945 by two of the Maislin brothers who began by transporting fish to New York and returning with fruits and vegetables. Maislin expanded to become Canada's largest highway carrier, the eighth largest trucking company in North America,[2] and the largest North American international carrier.[3] Maislin's shares were opened to public trading in 1972,[4] although they remained closely held. The company was 80 per cent owned by the Maislin family at the time of the bailout.[5] Through an agreement Samuel, Sydney, and Saul Maislin and Clément Beauregard held 79 per cent of the voting rights.[6]

Maislin experienced steady growth until 1976 when it first began to encounter financial difficulties. At this point Paul Des Rochers, former chief advisor to former Quebec Premier Robert Bourassa, was brought in to streamline management. He diagnosed 'chronic nepotism' as the major source of the company's difficulties.[7] By October 1978 management was reorganized and the company was in the black. (Des Rochers remained on the board of directors until the fall of 1981). In 1979 Maislin reported $3 million profit on $136 million worth of sales measured in Canadian dollars.[8]

By 1980 Maislin was again experiencing financial difficulty. On the eve of the deregulation of the American trucking industry which was carried out under the Motor Carrier Act of July 1980, Maislin had purchased two American trucking companies in an effort to improve its

competitive position. Unfortunately, deregulation (which Maislin apparently had not expected to occur as soon as it did, although most observers in the industry realized that it was very much in prospect) arrived when North America was experiencing an economic recession, high interest rates and rising fuel costs. As deregulation took effect in the United States, the industry found profit margins were increasingly squeezed by the increased price competition.[9]

Maislin's carrier network extended through the Eastern United States (east of the Mississippi), Quebec, Ontario, and the Maritimes. In 1979 the purchases of Gateway Transport of Wisconsin and Quinn Freight Lines of Massachusetts doubled Maislin's size. Maislin paid $11 per share for Gateway when it was trading at $4. Alan Maislin, then president of Maislin Industries, stated that opportunities for growth in Canada were limited, and that Gateway 'looked like a good deal at the time.'[10] Gateway added thirteen states and 22,000 route miles with 173 terminals to Maislin's network. It had a fleet of 4,240 vehicles and 3,300 employees.[11] It also came with a computerized billing system worth $3 million. However, unsuccessful attempts to combine Maislin's and Gateway's billing systems later cost the company sixteen weeks of billings. This moved Maislin from a cash to a borrowing position.[12]

Gateway had revenues in 1979 of US $147 million, and a loss of US $3.3 million. In 1978 the firm had lost $4.4 million ($1.55 per share). Maislin claimed to have cut Gateway's losses from US $2.4 million in the first quarter of 1979 to $1.6 million in the first quarter of 1980, but the integration of Gateway's operations with Maislin's make these figures difficult to verify. A similar turnaround was anticipated for Quinn Freight Lines which Maislin purchased for US $1 million. This was considered a 'fire-sale' price, and was payable over ten years in annual interest-free instalments.[13] Quinn added twenty-three terminals in the northeastern United States and the Maritimes to Maislin's network. In 1979 it had revenues of $13.7 million which permitted the company to break even that year. Quinn had been a source of major competition in the north eastern United States.

Maislin's expansionary moves occurred at what was to prove a poor time. The firm acquired excess trucking capacity based on an over-estimate of traffic growth. By 1981 it was crippled by interest payments of $12.5 million per year.[14] By September 1980 average truck tonnage was 17 per cent below 1979 levels.[15] To compound its problems Maislin had recently reached a costly wage settlement with the Teamsters union.

Over two years, wages were to rise 12.9 per cent and then 7.7 per cent.[16] While freight revenues had expanded rapidly during the 1970s, net earnings did not improve on the much larger asset and liability base. Chronic nepotism and the lack of hardnosed professionalism in management in the much larger and more complex operation are viewed by industry observers as major causes of the company's problems. (See financial and stock reports in Tables 24 and 25.)

LABOUR ISSUES

In 1982 Maislin had eighty-seven terminals in the United States and thirty in Ontario and Quebec. At the time of the loan-guarantee agreement with the federal government in July 1982, Maislin's workforce was 4,000, with 2,000 employees in the United States, 1,500 in Montreal, and 500 in Ontario;[17] although the exact distribution of the workforce between Canada and the United States was a matter on which governments had a great deal of difficulty obtaining information. This was a drop from Maislin's total workforce level of 5,862 on 31 December 1980.[18] A large proportion were American since 93 per cent of Maislin's business occurred in the United States using American employees.[19] Herb Gray stated that 92 per cent of Maislin's revenues were derived from its US operations or US-Canada transborder operations.

Stephen Flott, executive vice-president of the Ontario Trucking Association at the time of the bailout, minimized Maislin's importance to Canadian employment. Flott stated that Maislin licenses could quite easily have been picked up by other firms or drivers and employment would have been maintained. As an alternative to a bailout, Flott asserts that for a fraction of the cost to the government, other major Montreal-based carriers could have been persuaded to take over Maislin's operations and that with limited government financial assistance there would have been an orderly reduction in any temporary excess capacity in the merged firms. In addition, other Canadian trucking companies could have used their excess capacity to pick up the slack.[20] Flott maintained that Canadian funds were used to support American jobs, and that Canadian truckers were left with excess capacity when Maislin was salvaged. There are many thousands of trucking companies in Canada operating at less than full capacity.[21] American traffic alone had fallen 17 per cent since 1979.[22] However,

TABLE 24

Financial statistics (ten year summary)[b]

	1982	1981	1980	1979	1978	1977	1976	1975	1974	1973	1972
Revenues	195,737	293,479	285,815	116,097	117,724	101,962	96,772	84,062	86,087	79,773	48,577
Income taxes (recovery)	935	(3,104)	(1,840)	1,170	667	(691)	251	340	967	1,313	2,023
Net earnings (loss)	(19,866)	(12,723)	(13,788)	2,245	1,055	92	(446)	959	529	3,447	2,389
Common shares outstanding	2,516	2,516	2,516	2,516	2,516	2,516	2,516	2,512	2,475	2,460	2,458
Net earnings (loss)[a] per common share[b]	(7.89)	(5.06)	(5.48)	.91	.42	.04	(.18)	.39	.21	1.40	1.02
Total assets	89,935	113,116	158,325	83,010	83,840	71,366	75,970	72,002	71,964	64,774	39,130
Working capital (deficiency)	(14,284)	(30,483)	(16,861)	8,424	4,934	1,356	1,589	3,833	1,012	1,521	3,812
Cash flow (deficiency) from operations	(13,096)	(3,892)	785	8,754	6,576	5,520	6,206	7,358	6,070	5,803	5,365
Net capital expenditures (disposals)	n/a	(5,788)	4,609	9,998	11,704	1,608	8,173	4,161	15,452	12,303	4,725
Long-term debt	n/a	36,697	56,765	32,934	37,578	28,743	33,085	33,259	33,743	24,743	15,375
Shareholders' equity	(23,710)	(3,844)	8,879	22,728	20,590	19,553	20,092	20,508	19,078	18,460	16,710
Number of shareholders[a]	n/a	1,251	1,370	1,416	1,498	1,585	1,638	1,656	1,310	1,180	1,006

TABLE 24 (cont'd)

	1982	1981	1980	1979	1978	1977	1976	1975	1974	1973	1972
Number of employees[a]	6,000	4,212	5,862	2,585	2,518	2,747	2,852	2,853	3,175	3,358	2,202
Wages and benefits	n/a	169,975	183,517	64,905	68,896	59,890	56,618	47,772	48,705	42,705	23,908
Freight revenue	n/a	285,845	277,530	108,820	111,093	96,268	89,796	77,930	79,778	73,897	43,261
Shipments handled	n/a	2,005	2,783	928	928	973	1,025	942	994	1,225	697
Tons handled	n/a	3,316	4,158	1,769	1,996	1,987	2,007	1,819	1,987	2,075	1,185
Tons per shipment[a]	n/a	1.65	1.49	1.91	2.15	2.04	1.96	1.93	1.45	1.69	1.70
Revenue per shipment[a]	n/a	142.57	99.72	137.37	119.74	98.98	87.62	82.73	80.29	60.32	62.07
Revenue per ton[a]	n/a	86.20	66.75	77.06	55.66	48.46	44.75	42.83	40.14	35.61	36.52
Motor carrier terminals[a]	n/a	78	117	38	38	38	38	39	40	43	28
Revenue equipment:[a]											
Powered	n/a	1,627	2,405	973	994	1,169	1,242	1,193	1,331	994	869
Trailers	n/a	3,405	5,426	2,603	2,742	2,754	2,784	2,715	2,735	2,092	1,475
Total	n/a	5,032	7,831	3,576	3,736	3,923	4,026	3,908	4,066	3,086	2,344

a All figures are expressed in thousands except where *a* appears.
b 1979, 1980 and 1981 are expressed in United States dollars; all other years are expressed in Canadian dollars.
SOURCE: 1981 financial statements and 1983 *Financial Post* Survey of Industrials.

TABLE 25
Maislin share prices

Fiscal year	Common shares		
		Price range (Cdn.$)	
	Earnings per share[a]	High	Low
1982	US $ (8.71)	–	–
1981	US $ (4.83)	4.75	1.20
1980	US $ (5.16)	6.00	4.00
1979	Cdn.$ .91	6.50	3.85
1978	Cdn.$ 0.42	4.70	2.60
1977	Cdn.$ (0.08)	3.50	1.90
1976	Cdn.$ (0.20)	4.40	2.00

a Before extraordinary items.
SOURCES: *The Financial Post* Corporation Service 24 November 1982 and 4 January 1983.

Herb Gray repeatedly asserted that Maislin's bankruptcy would be a blow to an already severely depressed Montreal labour market.

As Maislin declined in 1980 it attempted to cut wage costs and raise funds to meet interest payments of $12.5 million per year through a 'job security and profit participation plan'[23] initiated in June 1981.[24] Maislin sought voluntary loans totalling 15 per cent of gross wages.[25] At this time clerks were earning an average of $300 per week while top drivers earned $700 per week. Frank Seligman, then Maislin's vice-president of Corporate Affairs, predicted that if all employees had participated the loan could have saved the company a total $1.8 million per month.[26] Repayment was to depend on future profits. Employees would have received 33⅓ per cent annual interest on the loan if adequate funds, an undefined term, remained after paying back capital. Maislin was not the first company to propose such a scheme.[27]

However, the Teamsters union which had originally agreed to recommend acceptance of the 'loan'[28] decided to inform employees that leadership opposed the plan.[29] Charles Thibeault, president of the Ontario Joint Council of Teamsters and of Local 938 in Ontario, joined with the local leadership of Ottawa, Hamilton, and London, Ontario in rejecting the wage cut. They argued that the company wanted an interest-free loan with no guarantee of repayment. The Teamsters maintained that

only the company could gain from such an arrangement, and it was unlikely that the company would fail without it.

Maislin's plan also met with difficulty under regulations of the Quebec Securities Commission. The QSC opposed the employee loan, stating that it was a securities offer and must be registered as such or Maislin must seek an exemption. The 'loan' constituted an interest in capital assets, gains, or profits since it was to be repaid with future earnings. Maislin sought an exemption and received one in late July 1981. Almost $3 million was eventually raised through the plan.[30]

Pressure for contract concessions by employees was occurring throughout the trucking industry. In September 1981 the US Teamsters agreed to reopen negotiations on the National Master agreements six months early. They had rejected a similar request one month earlier but now conceded that deregulation was having a devastating effect on the 300,000 members of the Teamsters covered by the agreement. Since August 1980 some 416 master carriers had gone out of business and from 18 to 24 per cent of the union's members were laid off.[31] Their average wage at this time was slightly under $13.00 per hour, excluding fringe benefits which increased real wages by approximately 30 per cent.

A tentative agreement was reached on 15 January 1982 which provided for changes in work rules and an annual rather than semi-annual cost-of-living allowance (COLA). This was expected to save the industry $100 million and put 50,000 people back to work.[32] In late April, however, continued weakness in the industry led employers to press for more concessions in the United States. It was thought that the union would make selective concessions, company by company, to try to prevent more layoffs. The union was adamant, however, against taking any more wage cuts under the master agreement.[33]

THE BAILOUT

Debate

Following its approach to employees for pay cuts, Maislin made a request to the Canadian Imperial Bank of Commerce for a loan. The request was refused and Maislin approached the federal government for assistance.[34] Maislin made a formal application for federal aid in early July 1982 under the Enterprise Development Program (EDP) which is administered by the Department of Industry, Trade and Commerce (ITC). (One of the purposes of the EDP is to provide assistance on a last-resort basis to help

the restructuring of companies where the goal is long-term viability.) An informal approach appears to have been initiated at an earlier date. In June 1982 the *Montreal Gazette* reported that preliminary discussions on the matter already had occurred in cabinet meetings [35]. This report may have been the result of a leaked ITC document.

Key private-sector actors in the bailout process were Alan Maislin, president of Maislin at the time of the bailout and then company treasurer, and Richard Skillinger, post-bailout president and chief executive officer. Charles Bronfman, president of Seagrams Company and co-owner with Maislin of a warehousing operation, was also widely identified as a lobbyist for Maislin. Charles Thibeault, president of the Ontario Joint Council of Teamsters and of Local 938 was the main union participant. Stephen Flott, then executive vice president of the Ontario Trucking Association, and Ken Maclaren, executive director of the Canadian Trucking Association, were the chief industry spokesmen.

Herb Gray, then Minister of Industry, Trade and Commerce, Alan MacEachen, then Minister of Finance, Jean-Luc Pepin, then Minister of Transport, Marc Lalonde, then Minister of Energy, Mines and Resources, Pierre de Bané, then Minister of State for External Affairs, and then Prime Minister Pierre Trudeau were the active cabinet members. Pierre de Bané was apparently the major advocate of support for Maislin, strongly supported later by Marc Lalonde. Don Johnson, President of the Treasury Board, and Treasury Board and ITC officials were strenuously opposed. According to one cabinet source, throughout cabinet discussions in June over Maislin's fate, 'there was blood and gore on the Cabinet room table at practically every meeting of Planning and Priorities'. According to a top Liberal political backroomer, from a political standpoint the Maislin bailout was one of the most serious mistakes the Trudeau administration made.

Involved opposition MPs were Pat Nowlan, Conservative transportation critic and Michael Wilson, industry critic. The NDP played a minimal role. Provincial governments were inactive, surprisingly so in the case of Quebec since Maislin was based in Montreal. The US government played no direct or overt role although it was alleged that Washington's silence over the proposed bailout of a firm in competition with American trucking companies could only indicate that the bailout was not strenuously opposed in the United States.[36] In part perhaps because of the severe difficulties in the US industry at the time, the

proposal to subsidize a Canadian carrier with US operations apparently was not considered particularly significant relative to other concerns.

Political opposition during the decision-making process was limited due to an information vacuum. The policy process was characterized by secrecy. Criticism from the Conservative party centred on demands that economic factors, rather than Liberal political fortunes in Montreal, be the deciding issue in granting assistance.[37] The rescue of a service industry would require a change in ITC regulations governing the EDP which had not been designed to assist the service sector. Such a change would have established a precedent and opened the door to all service industries to seek federal assistance. Pat Nowlan MP challenged Jean-Luc Pepin, then Minister of Transport to 'admit that the real reason consideration is being given for the perversion of the EDP program is political pressure from his political friends'. Pepin replied that services are just as useful in society as manufacturing, and the interest in helping Maislin was essentially the maintenance of employment in Quebec, and the maintenance of a US-Canada trucking service. Pepin claimed that the government had previously helped a number of service industries, although he declined to name those which had received aid.[38] Herb Gray added that any service industry receiving aid must have proven itself essential to the manufacturing and processing sectors.[39] He was proposing amendments to the EDP regulations to permit service industries to qualify.

Within the trucking industry, opposition to a Maislin bailout was intense. Both the Canadian Trucking Association[40] and the Ontario Trucking Association stated that the industry was opposed to government aid on principle.[41] With excess capacity in the industry, marginally more healthy companies would not survive without some failures. A group of unnamed trucking officials claimed that Maislin was being treated as a special case because it was based in the Liberal stronghold of Quebec. J.C. Carruth, president of Alltrans Canada Inc., claimed that the bailout would serve to aid an essentially American company and its US employees and creditors, since the majority of Maislin's operations were in the United States.[42] He forecast that a large number of firms would submit further requests for aid. One veteran industry observer told the authors that 'the Maislin fiasco was unquestionably about the saddest experience I have had in my [many] years in the industry'.

Industry, Trade and Commerce officials soon revealed that Maislin was indeed one of several trucking companies requesting assistance.[43] J.R. Ellis, Conservative MP, questioned what criteria would apply to other trucking companies seeking aid.[44] He claimed that the guarantee to Maislin would cost five times the rate per job spent for guarantees to Chrysler and Massey Ferguson.[45]

In late June 1982 a report of ITC and the Department of Regional Economic Expansion (DREE) termed Maislin 'technically bankrupt', in part due to poor management practices, including overexpansion.[46] A bailout would not solve its long-term problems, and Maislin's security would be inadequate to cover the loan. Maislin was assessed as a poor risk for loan guarantees.

The loan-guarantee agreement

Ottawa's policy decision was announced publicly in an ITC press release on 9 July 1982. Maislin was offered $34 million in federal loan insurance as part of a total aid package of $55 million.

In a final agreement signed on 13 September 1982 the Canadian Imperial Bank of Commerce played the largest role in the refinancing venture. It provided a credit facility of a maximum of US $55 million including an operating credit of $10.5 million, a term loan to Maislin Transport of Delaware of $6.9 million, a term loan of $5.1 million, a convertible income debenture of $17.5 million (the conversion was to a fifteen-year term loan which was to convert into a ten-year term loan on 31 July 1987), and a two-year revolving convertible credit not to exceed $15 million. (The conversion was to a fifteen-year term loan on 1 August 1981. The loan matured on 31 July 1999). If the convertible credit was not used by 31 December 1983, it would terminate.[47]

Ottawa and the Canadian Imperial Bank of Commerce entered into an insurance agreement covering 90 per cent of any exposure the CIBC might incur as a result of loans provided under the $17.5 million income debenture and the $15 million convertible credit (only if the aggregate amount of the insurance with respect to the income debenture was limited to $13.5 million). Interest on all the loans was payable at prime plus 1 per cent. Interest on the $17.5 million income debenture was payable only to the extent that Maislin's profits were sufficient to cover interest. Any accrued interest owing if and when the income debenture ceased to qualify under the Income Tax Act would be extinguished and

Maislin and Ottawa would be relieved of any obligation to pay the interest shortfall to the CIBC.

An 'income debenture' is defined under the Income Tax Act as a bond or debenture in respect of which interest or dividends are payable only to the extent that the issuing corporation has made a profit before taking into account the interest or dividend obligation. It must be issued

> (c)for a term that must not, in any circumstances, exceed 5 years, in the case of issuing corporations resident in Canada
> (iii)and at a time when by reason of financial difficulty. . .[48]

The five-year period in Maislin's case would give the company until 1986 to improve its performance and thus meet its interest commitments to the CIBC.

The conditions of the guarantee did not include job guarantees. There appears to have been an assumption by Ottawa that an implicit guarantee would ensure the maintenance of the Canadian employment level at 2000. The Teamsters had originally agreed to persuade locals to accept the '6 and 5' wage guidelines of the agreement.[49]

Existing shareholders agreed to increase equity by \$2.5 million. However, this was not fresh equity. It was later discovered that the entire \$2.5 million had been raised through the liquidation of a pension plan at Gateway.[50]

Maislin had also agreed to strengthen its management. The government secured the right to approve the appointment of a new chief executive officer acceptable to Ottawa, the CIBC, and Maislin. Richard Skillinger was appointed[51] after being interviewed by federal officials.[52] In addition, Maislin was to name a new full-time vice-president, finance. This responsibility had previously been carried by an outside consultant, retained on contract by the company. Ottawa also obtained the right to appoint a nominee to the board of directors (although it encountered severe difficulties in finding anyone knowledgeable about the trucking industry who was prepared to act in this capacity). However, Ottawa was not entitled to issue directives to management or to dismiss the CEO. The real operational control acquired by the government under the agreement appeared to have been limited.

Ottawa also received the option to purchase 15 per cent of Maislin's common stock for \$1. It could be acquired at any time during the life of the loan guarantee and within two years after the loan guarantees'

demise. The CIBC negotiated an option to purchase 10 per cent of common stock for $1. Maislin had the first right of refusal to repurchase in both cases. Neither Ottawa nor the CIBC exercised its stock option.

Under the terms of the guarantee Maislin was to prepare quarterly and monthly financial statements for ITC.

IMPLICATIONS OF THE BAILOUT

Economic implications

As part of the loan-guarantee agreement Maislin had made a written commitment that it and its Canadian subsidiaries would adhere to a 6 and 5 restraint program for two years[53] with respect to unionized and nonunionized employees. Michael Wilson tied the provision by which Maislin would 'escape' interest payments on 50 per cent of its loans (almost $24 million) for two years with the provision for low wage increases.[54] Wilson stated that the Maislin deal was grossly unfair in an industry with marginal profits in which Maislin's competitors might face 25 to 30 per cent increases in gas costs, and high interest and wage bills.

In September negotiations were to begin between Maislin and its Ontario workers. The company expected the union to abide by the '6 and 5' condition of the loan guarantees because this condition had been accepted by the National Teamster leadership. At that time a nine-week strike was in progress between the Teamsters and the Motor Transport Industrial Relations Bureau in Ontario. Maislin (Ontario) had previously bargained as part of this group. The 3,500 truckers from the twelve different companies wanted wage parity with the large firms of Kingsway and Overland. Their settlement was close to double '6 and 5'. Charles Thibeault, the chief negotiator for the Teamsters, announced that Ontario Maislin Locals were rejecting '6 and 5' and that they were not going to let Maislin set the pattern for other negotiations.[55] He also stated that if Maislin came to the bargaining table with a predetermined position it would be bargaining in bad faith.

A two-and-one-half year agreement was finally reached in April 1983. Although it was within the '6 and 5' guidelines in the first two years, in the subsequent half year it provided for a total increase of 26 per cent over the life of the contract.[56] The average hourly wage would have increased by $2.75, from $10.39 in September 1982 to $13.14 in October 1984. Although it claimed that the contract violated the spirit of the '6 and 5' guidelines through its use of 'backend loading', Ottawa did not

terminate the loan agreement. The company denied that the wage contract contravened the guidelines.[57]

During 1982 Maislin enjoyed a degree of improvement. Its losses for the third quarter of 1982 were lower than in the parallel period in 1981. However, on 9 September 1982, the Ontario Securities Commission again suspended Maislin shares from trading pending compliance with Toronto Stock Exchange requirements respecting financial disclosure and the holding of an annual meeting.[58] On 12 July 1982 the OSC had issued a temporary order to halt stock trading for fifteen days because audited annual statements for the year ended 31 December 1981 and for the first quarter ended 31 March 1982 had not been filed with the OSC and delivered to holders of securities of Maislin as required by the Ontario Securities Act. As a result current information on the affairs of Maislin was not available to the investing public. This followed Maislin's request of 28 July 1982 that trading be suspended on the Montreal and Toronto Stock Exchanges pending an announcement. The value of Maislin's shares had been falling and had last been quoted in the range of 80 cents to $1.70.[59] Apparently, Maislin wished to halt speculation on its future until a bailout decision was made. A precedent had been set in June 1981 when Maislin halted trade amid rumors of bankruptcy; twenty-four hours later it made the request for wage loans.[60] On 12 August 1982 the Alberta Securities Commission also halted trading in Maislin stock for failure to file financial statements.[61]

Reactions from the trucking industry to the bailout were negative. Ken MacLaren, executive director of the Canadian Trucking Association, announced that he was 'incensed' at the bailout.[62] The Canadian trucking industry had 'nose-dived' in the first quarter of 1982, and almost all carriers were losing money. The bailout of Maislin appeared inequitable.

On 6 August 1982, shortly after the bailout announcement, Stephen Flott issued a press release condemning the bailout as a distortion of the industry. He reiterated his pre-agreement stance that Maislin had more American than Canadian employees, and added that certain problems would arise in the trucking industry as a result of the government's actions.[63] He expressed concern that interline carriers which were unsecured creditors were not sheltered from problems, and other suppliers were not protected. The OTA questioned how the government would deal with Maislin's competitors which were not given a two-year interest-free holiday, and whether the Teamsters union would agree to stay within '6

and 5' for other firms. Flott also wanted to know how other trucking companies could apply for assistance.

Requests to Ottawa for aid were made by a number of other trucking firms, perhaps primarily to embarrass the government. Thibodeau Finch Express Ltd., owned by Ontario-based Algoma Central Railway, applied immediately after the Maislin bailout. Chairman H. Jackman, a prominent Conservative, stated 'why should Algoma stick its neck out when Ottawa can?' A Toronto-based company, Henrie and Co., also made a request for help.[64] The fate of these applications is not known. When Ed Lumley took over as Minister of ITC from Herb Gray in the summer of 1982, he found that there were literally thousands of service-sector applications for assistance filed with the Department, including several inquiries by trade associations on behalf of their entire membership. On this being reported to Cabinet, apparently a decision was made to suspend any move to extend the EDP to the service sectors.

Political implications

Political reactions to the bailout were strong. Pat Nowlan, then PC transportation critic, stated that the guarantee was in effect a two-year interest-free loan of $19 million. He questioned how the government managed to obtain the agreement of the CIBC. Nowlan postulated that the Maislin agreement was the 'stick' to the 'carrot' of government aid to alleviate the CIBC's problems with Dome.[65] Marc Lalonde denied this allegation.

Perhaps the potentially most explosive issue is that of political patronage, the allegation of which again was made first by Pat Nowlan. The Progressive Conservatives claimed in the House and in public that Maislin received the guarantees only because company officials and contacts are friends of the Liberals.[66] On 3 August 1982 Nowlan asked Prime Minister Trudeau if he had checked with his ministers to find out if any of them had received representations from Charles Bronfman.[67] Trudeau replied that he would not reply because Nowlan had just said he would not believe the answer.

Bronfman is the president of the Montreal-based Seagram Company. He and Maislin Industries are co-owners of a warehousing operation in LaSalle, Quebec which services both the truckers and Seagrams.[68] Bronfman is also a known Liberal supporter and partner with Sydney Maislin in the Montreal Expos and the Montreal Concordes. Bronfman

had allegedly lobbied Pierre de Bane and Marc Lalonde to press for the bailout. He allegedly lobbied the Prime Minister during the 1982 All-Star game when Trudeau was his guest. There was also speculation that Herb Gray expressed limited opposition to the idea at cabinet meetings since he had succeeded in securing bailout assistance for Chrysler in Windsor.[69]

Opposition politicians criticized the government's lack of action towards the financial difficulties faced by small business.[70] Their concern was with a possible misallocation of government funds in a time of restraint. At the time the government repeated that Maislin's bailout was a loan guarantee, not a loan, and, to date, had not cost Ottawa any funds. The Maislin issue was rekindled during the debate on both the Old Age Security Act and the Retirement Benefits Act. Opposition members questioned how the government could spend millions on bailouts and yet refuse to index pensions.[71] The basic criticism by the Progressive Conservatives was that they could discover no economic rationale for this bailout because the employees could have been employed by other firms. With the entire industry in trouble Maislin appeared to be an odd company to rescue; its serious financial troubles were caused in part by poor management practices, such as the purchase of Gateway.

The post-assistance government-firm relationship was reportedly close. Ed Lumley stated that the government had not appointed a nominee to the board of directors because it had not found a knowledgeable, willing businessman without a conflict of interest.[72] A government official stated that federal representatives spoke with company executives almost every day and saw them approximately twice per month.[73] In addition the company prepared monthly financial statements which were not made public. Prior to his appointment, Richard Skillinger was interviewed by the government which also approved the appointment of a new vice president, Finance. The official stated that there was a fear that should the bailout fail it would become a 'political football'.

THE FAILURE OF THE LOAN-GUARANTEE AGREEMENT

As early as May 1983 it was reported that Maislin was in serious trouble and seeking more loans from its bankers. Government sources indicated that Maislin's detailed financial position indicated that it needed further aid. However, the company had not requested assistance since it had been aware that none would be forthcoming. Richard Skillinger

continued to assert that Maislin would turn around and planned 'to develop the bridge financing necessary to meet working capital needs'.[74]

On 23 June 1983 Maislin held its annual meeting from which members of the press were banned. However, its annual report dated 31 May 1983 was made available to the Montreal Stock Exchange. It revealed that Maislin had a substantial working-capital deficiency and had reported losses of $4.2 million in the first quarter of 1983. Alan Maislin refused to comment on the report and denied that Maislin was on the verge of receivership.[75]

On 8 July 1983 it was announced that Maislin had filed a 'proposition for bankruptcy in Canada, and for a Chapter 11 reorganization in the US'[76] Maislin had exhausted the $34 million in loan guarantees. (A Chapter 11 notice prevents seizure of a company's assets while a court considers a reorganization proposal.) On 12 July Maislin announced that it was laying off 80 per cent of its remaining 3,500 employees,[77] and that 95 per cent of operations would be closed within a week.[78] Only 750 employees would be retained in Canada and the United States during the company's attempted reorganization.[79] Maislin halted all pickups and deliveries, and was out of cash for operations.

Maislin's major subsidiaries, Maislin Transport Delaware Inc. of Detroit, International Trading Co., and three other affiliates filed holding proposals through bankruptcy trustee Richter and Associate of Montreal, the appointed trustees for Maislin Industries Ltd. A moratorium until 31 October 1983 was requested on all debt payments.[80] In Canada, Maislin was protected against creditors up to the time of the creditors' meeting of 17 August 1983 which was to consider the moratorium proposal. Under the Chapter 11 filing in the United States, the US subsidiaries were protected for four months.

There were approximately 2,000 Maislin creditors in Canada and the United States including more than 1,500 unsecured creditors.[81] Unsecured creditors were owed $18.3 million, while secured creditors were owed $59.4 million. This included debts of almost $40 million to the CIBC and $7 million to the National Bank. Major amounts were owed under liens on rolling stock. Preferred creditors were owed $5.6 million, and there were contingent or other liabilities, including cargo loss, damage claims, and the bank debts of affiliates which were guaranteed by Maislin, totalling $14.7 million.

Assets shown included book debts and advances to affiliates totaling $56 million, including US $38 million advanced to Maislin Transport

Delaware Inc. In addition, there was machinery, equipment, and rolling stock worth $4.9 million, real estate at a net book value of $5.9 million, and affiliates' investments of $5 million. Reported debts totalled $98.26 million, and assets totalled $75 million.[82]

On 13 July 1983 five Quebec Superior Court bailiffs seized eighty tractor trailers from the LaSalle terminal on behalf of leasing companies.[83] The CIBC also called its loans to Maislin through its appointed receiver, Clarkson Co. of Montreal.

In a further development, a group of Maislin employees seized twenty-five tractor trailers.[84] This was in retaliation for the bank's failure to honour their final pay cheque once the holding proposal was filed under the Bankruptcy Act. Under the Act employees are considered preferred creditors, and can only hope to recover $500 each. It is of note that changes in the Bankruptcy Act, which would elevate employees to the position of secured creditors for up to $4,000 each in unpaid wages, are stalled at second reading in the House of Commons. The trucking industry takes the view that if these changes were in force, other secured creditors in situations like Maislin's would put the company into receivership at the first sign of trouble to limit the claims of employees, which in many cases in the trucking industry are apparently likely to exceed the net worth on fixed assets of the company. On 16 July 1983 Alan Maislin resigned as vice president and treasurer of Maislin, stating that he would lead the fight for the recovery of employees' wages.[85] Union officials have stated that they will sue Maislin's directors to recover an estimated $1.5 million which is owed to employees in salary and benefits.[86]

On 31 August 1983 Maislin's creditors met and voted to adjourn the creditors' meeting for sixty days to allow the trustees more time to draw up a reorganization proposal.[87] A five-man creditors committee was established with membership consisting of three union representatives, one representative of nonunionized employees, one representative of a major creditor, and one representative of US creditors with observer status. The committee may convene a creditors' meeting at any time if it feels secured creditors are not dealing fairly with secured assets and it may inspect all bank documents. Prior to the meeting the National Trust Company of Toronto Ltd., on behalf of the CIBC, seized the company's assets and terminated all employees. The employees were reinstated following the postponement of the creditors' meeting. National Trust Co. announced that it had accepted an offer from

Consolidated Freightways of Menlo, California to purchase Maislin's Ontario and Quebec trucking permits for US $7.32 million, subject to the approval of the Ontario and Quebec Transport Authorities, FIRA, and the creditors' committee.[88] Roland LeBlanc, assistant administrator with the Quebec Transport Commission, announced earlier that seven other trucking companies had applied for temporary permits to take over routes formerly operated by Maislin.[89] The major factor now affecting Canadian creditors is to what extent the debt due the Canadian parent by its subsidiaries can be realized.

In late October 1983 Maislin was voted into bankruptcy by its creditors on the basis of the Consolidated Freightways offer. FIRA approved the deal as 'of significant benefit' to Canada on 21 December 1983. Approval had been granted already by the Ontario and Quebec transportation authorities; the deal was ratified by the employees and creditors on 26 March 1984. Ratification by the employees had been a condition of the sale to Consolidated which had reserved US $1.6 million for Maislin's employees. In May 1984 employees received their cheques which average 37 cents on the dollar for outstanding wage, holiday-pay, and severance claims. An average of $2,070 was granted in compensation to each employee,[90] which is a larger settlement than the $500 employees are granted under Canadian bankruptcy law. Maislin employees have acknowledged that their wage claims are now satisfied in full.

Maislin's remaining assets, $7 to $8 million in real estate, are to be sold with the proceeds to pay the $55 million Maislin owed to the CIBC. The federal loan guarantee of $34 million will be called upon should the bank be unable to recover the full amount of its loans. It seems highly likely that the entire guarantee will be called, without possibility of indemnification.

Financial trend analysis

Up to and including 1979, Maislin was a marginally profitable firm (see Table 24). As of 1979 its liquidity ratios, as observed in Table 26, although not strong were acceptable. The return on assets (ratio 7) was low and from the components of this ratio (5 and 6), it is clear that the cause was not the asset turnover but the profitability relative to sales (5). The leverage ratio was relatively debt intensive but not excessive and the Z score was positive although not very large. The picture in 1979 is of

a marginally profitable company which could have financial problems in the future.

In 1980 the company grew dramatically increasing its total assets by approximately 100 per cent; the financing for this growth was through long-term debt as well as current bank loans. The operating results for 1980 were very poor (ratios 4, 5, and 7) – the firm had a loss of US $13,788,000. The leverage ratio increased dramatically not only by the increased use of long-term debt but also the reduction in shareholders' equity due to the loss. The Z score demonstrated that the firm was in financial distress and the deteriorating liquidity and coverage ratios suggested that creditors could face serious problems.

The financial results for 1981 showed some improvement with positive earnings before interest and taxes (3). However, earnings were insufficient to pay interest (the coverage ratio, 3, was less than unity and net income was negative, 5). The return on assets was poor due to poor profitability (5) on good asset turnover (6). The leverage ratio becomes very high and due to the loss in 1981 the book value of shareholders equity is actually negative. This explains why the leverage ratio becomes negative. The Z score remains negative and becomes larger. Against this financial background it is no surprise that the company's banker refused to provide Maislin with a bank loan late in 1981.

The poor results in 1981 and the inability to get additional bank financing led to the bailout during 1982. Since the bailout was effective in September 1982, it did not affect the operating results in any meaningful way. The profitability ratios, coverage ratios and liquidity ratios deteriorated during 1982. The Z score becomes even more negative. The improving leverage ratio is an anomaly since the increase in long-term debt in 1982 was accompanied by a larger negative shareholders equity due to the substantial loss in 1982.

TABLE 26
Maislin Industries Ltd. financial ratios

	1982	1981	1980	1979
1. Current ratio	.12	.04	.74	1.48
2. Quick ratio	.07	.001	.70	1.39
3. EBIT/(interest)	(.42)	.70	(.83)	1.83
4. EBIT/average total assets	(.04)	.07	(.06)	.11
5. Net income/sales	(.10)	(.04)	(.05)	.02
6. Sales/average total assets	1.93	2.16	2.37	1.55
7. (5) x (6) = return on assets	(.20)	(.09)	(.11)	.03
8. Debt/(common)	(3.07)	(11.51)	6.39	1.55
9. Z	(4.85)	(2.04)	(2.22)	.133

SOURCE: Financial Post Corporate Service.

NOTES

1 Maislin Industries Ltd.'s major subsidiaries included Quinn Freight Lines, Gateway Transport, Maislin Transport, Maislin Transport of Delaware Inc., Acquisition Corp., Richmond Cartage, International Trading Co. There are a total of twenty-six subsidiaries.
2 Industry, Trade and Commerce News Release 30 July 1982.
3 *Canadian Business* 30 September 1980, 53: 70-4.
4 Ibid.
5 *Globe and Mail* 31 July 1982.
6 *Financial Post Corporation Service* 24 November 1982.
7 *Toronto Star* 8 August 1982.
8 *Canadian Business* op. cit.
9 *Bus and Truck Transport* August 1982, 59: 8 13.
10 *Montreal Gazette* 4 September 1982.
11 *Canadian Business* op. cit.
12 *Montreal Gazette* 4 September 1982.
13 *Canadian Business* op. cit.
14 *Globe and Mail* 16 June 1981.
15 *Canadian Business* op. cit.
16 *Toronto Star* 18 June 1981.
17 *Hansard* 3 April 1982; Industry, Trade and Commerce news release 30 July 1982.

18 *Financial Post Corporation Service* 4 November 1981.
19 Ontario Trucking Association, statement by executive vice president Stephen Flott 6 August 1982.
20 Ibid.
21 *Hansard* 4 April 1982, Michael Wilson, PC finance critic.
22 *Globe and Mail* 16 June 1981.
23 *Toronto Star* 12 March 1983.
24 Further cost-cutting measures included: 1) the receipt of $8-$10 million from the sale of property including terminals, closure of nineteen line-haul domiciles (driver and equipment bases) and nineteen maintenance shops. (*Montreal Gazette* 20 June 1981); 2) In October 1982 Maislin sold its vehicle leasing subsidiary to the Quebec franchise holder of Budget Rent-A-Car. The subsidiary had lost US $5 million in the first six months of 1981 (*Montreal Gazette* 21 October 1982).
25 *Bus and Truck Transport* August 1982.
26 *Globe and Mail* 16 June 1981.
27 *Toronto Star* 12 March 1983.
28 *Globe and Mail* 16 June 1981.
29 *Toronto Star* 20 June 1982.
30 *Montreal Gazette* 20 June; 25 July 1981; 26 June 1982.
31 *Daily Labor Report* Bureau of National Affairs Washington 16 September 1981.
32 *Business Week* 1 February 1982.
33 *Business Week* 10 May 1982.
34 *Toronto Star* 12 March 1983.
35 *Montreal Gazette* 26 June 1982.
36 *Hansard* 30 July 1982.
37 *Hansard* 8 July 1982 Pat Nowlan to Jean-Luc Pepin.
38 *Hansard* 23 July 1982 Jean-Luc Pepin to Pat Nowlan.
39 *Globe and Mail* 29 July 1982.
40 *Hansard* 19 July 1982 Jake Epp to Jean-Luc Pepin.
41 *Montreal Gazette* 3 July 1982.
42 Ibid.
43 *Globe and Mail* 29 July 1982.
44 *Hansard* 30 July 1982.
45 *Globe and Mail* 22 October 1982.
46 *Montreal Gazette* 26 June 1982.
47 1981 Financial Statement Maislin Industries Ltd.

48 Income Tax Act 1980-81.
49 *Globe and Mail* 31 July 1982.
50 *Montreal Gazette* 12 October 1982.
51 Richard Skillinger was a US trucking industry executive who had had success in turning around Hemingway Transport Inc. of New Bedord, Mass. of which he was president *(Globe and Mail* 24 March 1983).
52 *Financial Post* 26 March 1983.
53 ITC news release 30 July 1982.
54 *Hansard* 4 August 1981.
55 *Globe and Mail* 1 October 1982.
56 30 cents per hour, 1 April 1983, 2.9 per cent; 30 cents per hour, 1 October 1983, 2.8 per cent; 30 cents per hour, 1 April 1984, 2.7 per cent; $1.85 per hour, 1 October 1984, 16.4 per cent (*Toronto Star* 21 April 1983).
57 Ibid.
58 OSC statement 8 September 1982.
59 OSC statements 28-29 July 1982.
60 *Toronto Sun* 22 June 1981.
61 ASC statement 12 August 1982.
62 *Financial Post* 14 August 1982.
63 OTA news release 6 August 1982. Maislin is no longer a member of the Motor Trucking Bureau.
64 *Montreal Gazette* 2 October; 5, 19 August 1982.
65 *Hansard* 4 August 1982.
66 *Montreal Gazette* 23 August 1982.
67 *Hansard* 3 August 1982.
68 *Montreal Gazette* 17 August 1982.
69 *Globe and Mail* 22 October 1982.
70 *Hansard* 3 August 1982 – Joe Reid (St. Catharines). A record 348 bankruptcies had occurred in June in Niagara – if there was money for Maislin, is there money for these companies?
71 *Hansard* 15 November 1982.
72 *Globe and Mail* 30 March 1983.
73 *Financial Post* 26 March 1983.
74 *Toronto Star* 2 June 1983.
75 *Globe and Mail* 24 June; 13 July 1983.
76 *Toronto Star* 9 July 1983.
77 Ibid., 12 July 1983.

78 Ibid.
79 Ibid.
80 Ibid.
81 *Globe and Mail* 13 July 1983.
82 *Toronto Star* 12 July 1983.
83 *Globe and Mail* 14 July 1983.
84 Ibid.
85 *Globe and Mail* 16 July 1983.
86 *Toronto Star* 25 July 1983.
87 *Globe and Mail* 18 August 1983.
88 Ibid.
89 *Toronto Star* 13 July 1983.
90 *Globe and Mail* 22 October 1983.

13
Dome Petroleum

BACKGROUND

In September 1982, Dome Petroleum Limited became another potential bailout in the growing list of government rescues of failing private-sector firms. The Canadian banks continued to roll over the $1.3 billion principal repayment on a monthly basis until 5 February 1985 when Dome's principal repayment was extended. To fully understand Dome's financial plight, it is useful to look at Dome's performance prior to and after the National Energy Programme (NEP). What follows is a chronological attempt at analyzing Dome within that context. In order to understand Dome's strategic planning, it is necessary to have a rudimentary knowledge of Ottawa's energy policy.

The National Energy Programme (NEP)

There was widespread concern regarding the degree of foreign ownership in Canada's energy industry and the lack of centralized national control over planning for exploration and conservation. Throughout the 1960s in Canada, there was a significant increase in economic nationalism. The major thrust of that movement was the claim that the enormous degree of foreign – principally US – investment in Canada was ultimately detrimental to the country. According to government figures, almost 80 per cent of oil-industry assets were foreign-owned, while almost 90 per cent were foreign-controlled.[1] The National Energy Board (NEB) was often criticized because of the widespread perception that oil companies exerted undue influence on NEB regulatory decisions. For example, Peter

Foster alleges that the NEB made many of its decisions 'on the basis of the submissions from the oil industry and the figures of the Alberta Energy Resources Conservation Board, which was itself closely identified with the industry'. By 1970, the Department of Energy Mines and Resources (EMR) was being transformed from a bureaucratic body of scientists and technicians into a policy-making department under the management of Jack Austin, Deputy Minister of EMR. Prior to the creation of OPEC, Jack Austin felt the main priority should be the creation of a state-owned oil company.[2] The seeds of government involvement with the oil industry were thus laid in the early '70s. The formation of Petro-Canada was to follow. After OPEC, the public became very suspicious of the oil industry because of the industry's strong profit record. In Canada, this suspicion was further heightened by the foreign domination of the oil industry. In October 1980, the government responded to these concerns by creating the National Energy Programme. Marc Lalonde was Energy Minister at the time. Lalonde's policy imposed higher taxes and royalties on the oil industry. In addition, there was a provision for a 25 per cent back-in on federal lands.

However, the most notable aspect of the NEP was the Canadianization programme. The federal government announced that its objective was to achieve 50 per cent Canadian ownership of the domestic oil business by 1990.[3]

What has been the effect of the National Energy Programme on the strategic planning of oil companies? To what extent was the NEP responsible for the failure of Dome? Certainly, Dome's agents are responsible for Dome's destiny. However, without the NEP, and other indirect forms of federal support, would Dome ever have charted the expansionary course that led to its downfall?

Generally speaking, it is safe to say that Dome's management was not shy about asking for favourable treatment from the government. A possible reason for this is because of Jack Gallagher's (chairman of Dome Petroleum) intense interest in the development of northern oil. Gallagher and Bill Richards (Dome's president) had a very close relationship with Ottawa. In fact, in 1975, Energy Minister Donald Macdonald had queried Gallagher on his (Gallagher's) possible candidacy for the head of Petro-Canada.

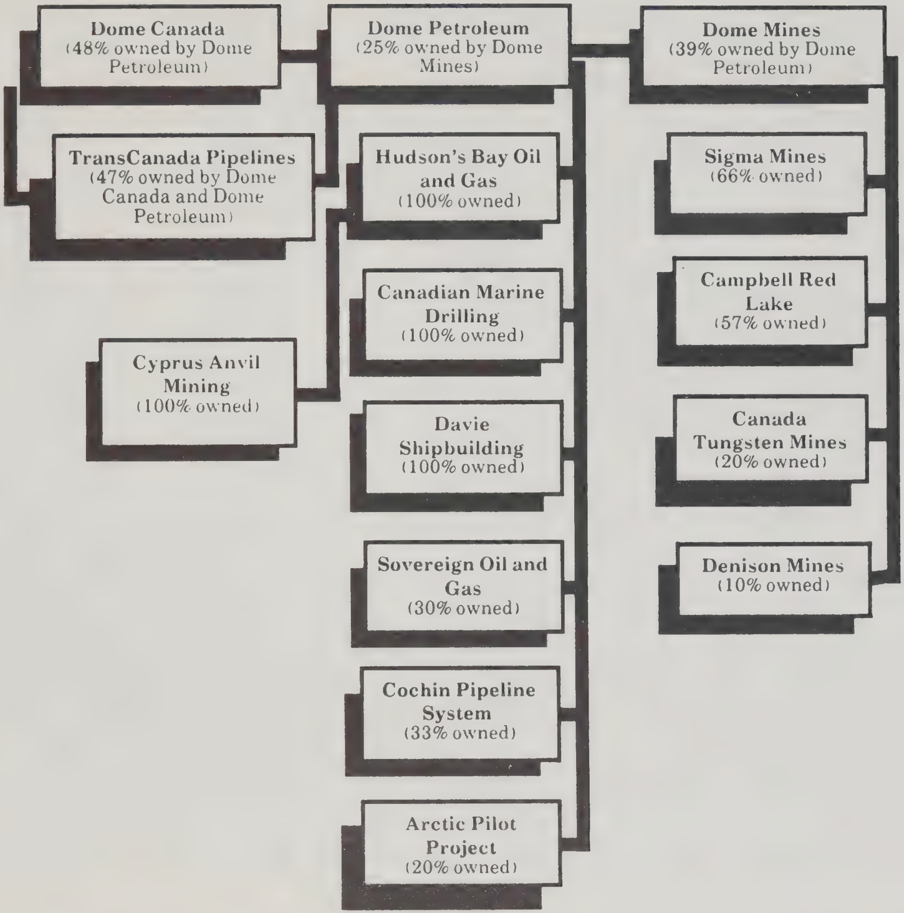
Dome Petroleum's formative period

Dome Petroleum was created in 1951. In that year, Dome Mines gave the oil company its name and funds for investment. In addition the Dome Mines connection provided Dome Petroleum with endowment investment funds from three US universities: Princeton, Harvard, and Massachusetts Institute of Technology.[4] The company grew rapidly under the chairmanship of Jack Gallagher. Figure 1 illustrates Dome Petroleum's corporate holdings in September 1982, prior to the proposed bailout.

Gallagher and Richards began their selling of the Beaufort Sea exploration project by pointing out that the Beaufort's alleged oil reserves were on federal not provincial lands. This fact exempted Beaufort from the federal/provincial dispute on pricing. The *Oil and Gas Journal* reported in 1980 that Richards had told the National Energy Board that half the Canadian crude would come from the Beaufort by 1990.[5] In 1981 Dome said oil would flow by 1986 if it could get approval from the Environmental Assessment and Review Agency of Transport Canada (Terminal Policy Branch), and the Department of Indian and Northern Affairs. Apart from how soon and how much oil would flow, Beaufort exploration had a potentially positive economic impact on the workforce. The development of Canada's far north has been a long-standing federal government objective. A 1980 *Fortune* article stated that, whereas winter crews amounted to 40 people, by mid-summer the workforce grew to 1,000. The projection was that when production peaked, 4,000 people would be working on the Beaufort oil rigs. Wages to these individuals were $2,250 per month for a cook, $6,250 per month for a driller, and $7,650 per month for the captain of a ship. In addition, the region benefited because 20 per cent of the workforce were Inuit.[6] Moreover, Gallagher stated that if Dome were allowed to keep funds (through tax relief and grants) and then spend it, those funds would turn over 3.3 times with a multiplier effect and the government would get more than the original tax dollar it would otherwise have received.[7]

Gallagher's personal lobbying efforts consisted of discussions with Pierre Trudeau, Jean Chrétien, Alastair Gillespie. and Donald Macdonald. The lobbying efforts won Dome their first subsidy. In the 1977 federal budget, finance minister Donald Macdonald introduced a super-depletion allowance. The allowance had generous tax writeoffs for wells costing more than $5 million. At the time, Dome was the only company drilling holes costing more than $5 million.[8]

FIGURE 1
Dome's corporate structure



SOURCE: Francis, Diane (1982) 'Sitting on a billion dollar time bomb'. *Toronto Star*, 12 September.

Dome has always been active in exploration for new wells. Dome reported that, both in 1979 and 1980, it set new records in Canada in exploration footage and in number of wells. In 1979 Dome reported that exploration represented 13 per cent of total Canadian footage. In 1980 Dome reported that exploration represented 11 per cent of total Canadian footage.[9] One of the reasons for this intense exploration activity was the super-depletion allowance. *Fortune* reported in 1980 that super-depletion, in combination with other tax incentives, allowed Dome to write off as much as 200 per cent of costs. In other words, $100 million in exploration costs sheltered $100 million in revenue from southern wells.[10] If super-depletion was removed the effect would be only 133 per cent in tax writeoffs and the high-cost northern wells would no longer be as attractive to investment planners at the oil firms. Super-depletion, also known as the Frontier Exploration Allowance was a tax deduction of $66\frac{2}{3}$ per cent for expenses in excess of $5 million. It was applicable to a company or individual from any source at any time. The remaining tax deductions came from the Canadian Exploration Expense (100 per cent) and the Earned Depletion Allowance ($33\frac{1}{3}$ per cent).[11] Because of the uncertainties and higher costs, oil companies needed some form of assistance to induce them to develop northern oil. Jack Gallagher was fond of mentioning the Hibernia well off the coast of Newfoundland as one of the major benefits to Canadians resulting from favourable tax breaks to oil companies. Chevron Standard admitted 'that it only drilled such an expensive wildcat because of the uniquely generous tax benefits of super-depletion'.[12] Super-depletion expired in March 1980.

1979-81

Dome's growth before the NEP

Dome's aggressive exploration record is also matched by its acquisition record. In June 1981 the *Montreal Gazette* reported that Dome's asset growth from 1976 to 1980 was 56 per cent compared to Imperial Oil's asset growth which was 19 per cent.[13] A chronology of Dome's 1979 and 1980 pre-NEP acquisitions follows.[14]

In May 1979, Dome bought additional shares worth $244 million in Trans-Canada Pipelines, bringing Dome's holdings in Trans-Canada to 48 per cent.[15] In May 1979 Dome increased its holdings in Dome Mines by purchasing another 8.5 per cent of the common shares. Dome now held 39.5 per cent of the outstanding common shares and was the

principle shareholder.[16] In January 1979 Dome bought a 76 per cent interest in Siebens Oil and Gas for $300 million.[17] In October 1979 Dome bought 60 per cent of Mesa Petroleum; *Saturday Night* reported the purchase price to be between $100 million and $200 million. In February 1980 Dome purchased 100 per cent of Kaiser Petroleum for $700 million. After the Kaiser purchase Dome had $2.9 billion in debt and an additional $500 million in deferred taxes. Dome's asset value at this time was $4.5 billion.[18]

The NEP is implemented

The Dome-Ottawa relationship was temporarily strained when Ottawa enacted the National Energy Programme in October 1980. The NEP adversely affected Dome whose foreign ownership would deprive it of lucrative exploration grants. Less than 50 per cent of Dome's shares were held abroad.[19] The NEP also hurt Dome by increasing the government's share of energy discovered on federal lands and by imposing higher taxes and higher royalties. Although Gallagher and Richards were powerless to do anything about taxes and royalties,[20] they did get a modification of the back-in clause. The 25 per cent back-in applies to all federal lands which, in turn, meant all Dome's Beaufort holdings. Although Gallagher's complaints to Lalonde did not result in retraction of the back-in clause, Dome was able to get compensation for the lands. The government agreed to 'make *ex gratia* payments for the back-in'.[21]

Dome's response to the 'Canadianization clause' was a crucial turning point in the company's fortunes. The rules for Canadianization meant that in order to qualify for the highest level of federal exploration grants a company would have to be 75 per cent Canadian[22] owned. These discriminatory grants were known as the Petroleum Incentive Payments (PIP). Dome had lost the benefit of the super-depletion and would now have to qualify for the PIP grants. Dome now had to take a fresh approach to qualifying for the government subsidies so that Dome could maintain its Beaufort effort.

Dome Canada is formed

The government encouraged Dome both directly and indirectly. At the end of January 1981 Energy Minister Marc Lalonde wrote a letter to Gallagher in support of Dome. The letter stated that he (Lalonde) would 'exercise the discretion which I expect the legislation (NEP) to provide'.[23]

By March 1981 Dome Petroleum had created a new company which would allow the firm to qualify for the maximum (80 per cent) grants available to Canadian companies as outlined in the PIP of the NEP. To meet the Canadian ownership requirements, Dome had to increase its Canadian ownership which was now at 35 per cent. Dome formed a new company called Dome Canada that would be owned 48 per cent by Dome Petroleum.[24]

The remaining 52 per cent of Dome Canada consisted of an all-Canadian issue of shares in the new company. The issue raised $434 million for Dome Canada and was sold to 60,000 Canadian investors. The Dome Canada share offering was the second most successful in Canadian history, coming very close to the $487.5 million raised in June 1979 by the British Columbia Resources Investment Corporation. Six per cent of the total issue was purchased by 2,800 Dome employees.[25] Because of its size and the Canadian ownership aspect, the Dome Canada issue was also a substantial undertaking for the Canadian investment houses. The investment industry earned $25 million in commissions from Dome deals.[26]

It was at this juncture that government discretion was exercised to Dome's advantage. It was felt that the biggest hurdle to the successful sale of Dome Canada shares was the fact that the NEP, on which the PIP grants depended, had not been enacted. Dome thus asked Lalonde to send a letter stating that Dome Canada would be eligible for the grants.[27] Lalonde sent the letter laying out the government's attitude toward Dome Canada and then gave permission for the letter to be printed in the Dome Canada prospectus.[28] In addition the Canada Business Corporations Act was amended to allow Dome to restrict its sale of shares to Canadians only.[29] Finally, the Canadian government again went to Dome's aid by accepting Dome Petroleum's figures regarding Canadian ownership. Calculating Dome's Canadian ownership using the government figure meant that the new company, Dome Canada, was only 67.75 per cent Canadian.[30] In order not to disrupt the government's progress toward energy self-sufficiency, the federal government changed Canadian Ownership Rules (COR) relating to how each company established its Canadian ownership. Since Dome Petroleum was the only oil company attempting to qualify for the PIP grants, the relaxation of COR aided Dome immensely.[31]

The oil industry joined the Progressive Conservatives in lobbying against the NEP and the preferential treatment for Dome. Sinclair

Stevens alleged that Energy Minister Lalonde wanted to change the Canada Business Corporations Act to aid Dome.[32] Liberal amendments would allow directors of any corporation under federal jurisdiction to buy shareholders out in order to qualify for a type of licensing which required a certain level of Canadian ownership. Stevens stated that it was hard to determine the Canadian ownership in Dome Petroleum since its shares are mixed up with Dome Mines (see Figure 1) which has partial foreign ownership.

Dome Petroleum's purchase of Hudson's Bay Oil and Gas (HBOG)

During this period when Dome Canada was being formed, Dome decided to take over Hudson's Bay Oil and Gas. As Peter Foster describes the HBOG purchase, Dome sought 'to outpace, rather than merely follow the thrust of the NEP', by launching the biggest takeover in Canadian history.[33] Dome had decided to get control of Hudson's Bay Oil and Gas from the US giant Conoco. In order to gain control of HBOG, Dome first had to acquire the controlling interest in HBOG. In May 1981 Conoco's shareholders accepted Dome's offer price of $65 per share. (In April 1981 Conoco shares had traded for $57 per share.)[34] After the shares were tendered Dome had purchased 22.5 per cent of Conoco's outstanding shares. The purchase price was US $1.68 billion or about $2 billion Canadian and Dome borrowed this amount from a group of Canadian banks. Dome then took the outstanding shares of Conoco and traded them for 52.9 per cent of Hudson Bay Oil and Gas. Dome's ante for HBOG was $50 per share.[35] After the purchase Dome's total debts stood at $4.8 billion. About $3.8 billion of its debt was at a floating rate which meant that Dome would pay a higher interest rate as the prime lending rate went up.[36] interest rates went from 14 per cent in 1980 to just over 23 per cent in September 1981.[37] Annualized interest on the $2 billion purchase was $387 million.[38] This was only slightly offset by $13 million in annual dividends paid by Hudson's Bay Oil and Gas.[39]

When Dome bought HBOG, it was 'essentially' buying:

1 Relief from high royalty rates – much of HBOG land was 'freehold land', which is land deeded with minimal rights established before Alberta was a province.

2 Land – HBOG had 5.6 million acres on the east coast (compared to Dome's 2 million acres) and 1.23 million acres in the Arctic.

3 Potential cash flow.

The *Financial Post* reported that Dome might possibly be buying an additional $338 million in cash flow since Dome was so adept at avoiding taxes.[40] Hudson Bay Oil and Gas paid $87 million in taxes in 1980.[41] In addition, Dome 'replaced Shell Canada Resources Ltd. as the number one producer of natural gas after its acquisition of HBOG'.[42] However, Dome would not have access to HBOG's cash flow until it acquired the remaining HBOG shares (47 per cent of the shares were in the hands of minority shareholders).

The US response to the HBOG purchase

The HBOG purchase had the effect of angering many interests. In the United States seven bills were introduced in the House and Senate as a response to several Canadian raids on US companies.[43] The US response was generally that Canadian banks were not required to limit their investment in any particular company as US banks were. Canadian firms might therefore find it easier to raise the capital to ultimately buy out American interests.[44] The US critics also argued that the National Energy Program was basically discriminatory and that it enabled Canadian companies to take over foreign-owned assets at distress prices.[45] Although it is debatable whether HBOG was sold at a distress price, Conoco shareholders were paid $65 per share and the shares had traded at $56 the month before.

A flurry of activity was occurring not only in Congress; the US courts were also involved in the adverse response to this Canadian purchasing activity. In the United States, Conoco sued Dome. However, a US District Court judge ruled that Conoco failed to meet the burden of proof necessary to show that: Dome's tender offer would inflict irreparable harm on Conoco shareholders and that Dome's financial statements contained omissions and misrepresentations.[46]

Dome Petroleum's buying spree continues

The effect of the original HBOG deal was a drop in stock prices. On 3 June 1981 it was reported that Dome Petroleum's shares had fallen $1.12 per share after the Conoco takeover.[47] Dome's assets had gone from $5.1 billion to $6.3 billion. Its debt had risen from $2.6 billion to $4.6 billion. Imperial Oil, with the same amount of assets ($6.3 billion), had one-tenth the amount of debt.[48] Undeterred by their debt loan and the market reaction, Gallagher and Richards continued to buy. Shortly after the first HBOG purchase, Dome purchased a small oil and gas company called Horn River Resources Ltd.[49] which later became a holding company called Canada Resources. In June, Gallagher and Richards proceeded to buy Davies Shipyard Ltd. for $38.6 million.[50] Gallagher was also considering building a new shipyard to supply twenty-five tankers and four icebreakers for the Beaufort. The cost of the proposal was $300 million for the shipyards and $200 million for each tanker.[51] Gallagher argued that with the lead time of two years required for the Beaufort ships, immediate expansion was essential.[52] Dome stock prices in June 1981 fell from $21 to $12 per share. Although Gallagher's buying strategies had little appeal to stockholders, they appeared to fit well with the federal government's desire to get northern oil on-stream as soon as possible.

In August 1981 Dome Petroleum continued its spending spree. Dome purchased an 87.5 per cent[53] controlling interest in Cyprus Anvil Mines (a company that mines lead and zinc) for $340 million.[54] This aquisition was assisted indirectly by the Foreign Investment Review Agency (FIRA). Cyprus Anvil was 63 per cent owned by Los Angeles-based Cyprus Mines Corp. but the US parent had been taken over by Standard Oil of Indiana and FIRA refused to let ownership of the Canadian subsidiary change too. Refusing transfer of ownership was one of FIRA's methods of forcing Canadianization of such subsidiaries. FIRA had been quite active in restraining further foreign ownership of Canadian energy resources. During the 1970s FIRA was used to discourage the major oil companies from any large oil company takeovers. Under the NEP, FIRA would be used 'to prevent foreign-owned oil companies from either diversifying outside the oil and gas business, or buying already discovered oil and gas reserves'.[55]

In November 1981 Dome moved to acquire the remaining publicly held minority interest in HBOG. It filed a prospectus for the issuance of

floating-rate preferred shares to be traded for each HBOG share. On 19 September, the *Globe and Mail* reported that the preliminary prospectus was withdrawn by Dome.[56] This false start created legal problems for Dome but Dome lawyers were successful in persuading the Ontario Securities Commission to waive regulations that would have required Dome to make an equitable counter offer to the remaining shareholders within 180 days of the first offer.[57]

Some analysts have suggested two reasons for the delay. First of all, Dome would have had to fully disclose its debt position to the OSC because more detailed information is required by them. Such disclosure might have resulted in a further drop in the price of its shares; Dome would have to part with more shares to match the share price of the stable HBOG shares. Secondly, Dome appeared to be waiting for optimistic news from the Beaufort (due in late September), in order to drive up Dome share prices and enhance its bargaining position.[58]

There was a great internal struggle regarding the timing of this equity issue. Peter Breyfogle, Dome's chief financial officer, argued that Dome should move immediately. Several factors were in Dome's favour. First, Dome's stock price was between \$23 and \$24. Secondly, Dome's second-quarter results were not supposed to be as encouraging. Third, Breyfogle wanted to prevent the remaining shareholders from holding Dome up for ransom. As long as a takeover of the minority shares was inevitable, the value of HBOG shares would increase. Fourth, by gaining the minority shares Dome would be able to sell off assets and improve its financial picture. Breyfogle was concerned, in particular, by a rise in interest rates and the growing evidence of an oil glut.

Effect of Beaufort exploration and the creation of Dome Resources

In late September, as expected, Dome announced its analysis of the recent assessments of its Beaufort drilling program. Dome forecasted that its average Beaufort well would produce 12,000 barrels per day; these projections were regarded by many industry experts as overly optimistic. Dome's experts countered by arguing that the results might be too pessimistic since the Beaufort data was so difficult to interpret.[59] During the first week of October, Dome Petroleum's shares fell to \$11 5/8 from the \$17 market price on 16 September.[60] Also, Dome Canada shares had fallen to \$4.60 (less than half their issue price).

On 5 November 1981, the *Globe and Mail* reported that the Beaufort results were still not conclusive.[61] Faced with a 21 November OSC deadline, Dome tendered on the remaining HBOG shares. Declining oil prices and rising interest costs were having a negative impact on Dome's share price. This made it difficult for Dome to raise additional cash in order to buy the shares outright. Therefore, Dome Petroleum transferred Horn River Resources Ltd. from Alberta to federal jurisdiction, and renamed the company Dome Resources Ltd. Dome Resources then offered one Dome secured retractable preferred share with a face value of $57.50 for each HBOG share tendered. All but 1,940 of the 39.4 million shares outstanding were tendered.[62] Each Dome Resource share also contained a warrant to purchase 1⅓ Dome Petroleum shares for $23.11 The Dome Resource preferred stock paid a 10 per cent annual cumulative dividend (payable each quarter).

The preferred shares were issued with a retractability provision which obligated Dome to repurchase the preferreds at a face value of $57.50 in three years time. In order to guarantee its financial ability to repurchase the shares, Dome Petroleum entered into a loan agreement with a consortium headed by Citibank of New York. The twenty-six participating banks agreed to loan Dome the funds it would require to purchase the preferred shares in return for a commitment from Dome to create a US trust fund to secure repayment of the loans from the consortium. The *Globe and Mail* reported this US loan was the largest ever granted to a Canadian company.[63] Because the Inspector General of Banks had expressed alarm at the Canadian banking community's exposure in oil companies, the Canadian banks were not interested in becoming more involved with Dome.[64] The necessity of financing the remaining 47 per cent of HBOG shares through debt rather than equity may have been Dome Petroleum's fundamental error.

In the meantime, Dome hired a Dallas consulting firm, DeGolyer and McNaughton, to interpret the Beaufort results. DeGolyer and McNaughton's reputation as petroleum analysts was attributable to the accuracy of its prediction of the Alaskan Prudhoe Bay discoveries. While generally favourable, the consulting firm's report failed to state conclusively that the Beaufort oil was commercially viable.[65] On 9 November 1981 Dome's stock fell another $1. It is not apparent whether this decline was due to the Beaufort results or the disclosure of the terms of the HBOG tender offer.[66]

To complete the tender offer, Dome was again to ask favours from the federal government. The previous federal budget had taken away the capital gains tax-exempt status for share exchanges. Richards pleaded with the Secretary of State, Gerald Regan[67] to 'grandfather' Dome in. Later, Finance Minister Allan MacEachen announced that certain tax advantages would be re-instated for businesses that had been re-organized prior to 21 November.[68] Dome met the 12 November criterion.

The aftermath of the HBOG takeover

The effect of the second stage of the HBOG takeover was a demand by Dome Canada's bankers for a restructuring of collateral. To attract the financial backing of the US banks, Dome had to convince the Canadian banks to give up their collateral in the HBOG Canadian oil and gas wells.[69] The Canadian banks had no choice. Dome insisted that it had to have HBOG cash flow and the Inspector General of Banks was unwilling to let the Big Four banks become more involved in Dome's financing. The US banks thus got the Canadian collateral. The Canadian banks responded by attempting to obtain security interests in other unpledged assets. During the period from the original 53 per cent purchase of HBOG in May and the subsequent 47 per cent tender for minority shares in November, the Canadian banks obtained security interests in virtually all Dome's unpledged assets. The effect of this further encumbrance was that Dome's ability to borrow additional funds was now close to zero. In addition, under the original terms of the Canadian bank loan to buy the 53 per cent of Conoco shares, Dome's loan was repayable on 31 January 1983 with an option to extend it for ten years. Now, the Canadian banks wanted their money by 30 September 1982.[70] Richards was told to start selling assets so he could pay them back. The completion of the second stage of the HBOG purchase did not resolve Dome's problems. Oil revenues were falling. But it was interest rates in particular that were beginning to cripple Dome; much of its debt was at a floating rate of interest. Of course, hindsight has a proven track record, but much of the literature suggests that Dome's strategy regarding equity was partially responsible for its interest burden. The company had big internal fights over increasing the number of shareholders. If Dome had gone into the equity market immediately to acquire the remaining 47 per cent HBOG interest, it could have reduced its debt commitment.

In September, Dome's serious problems with debt servicing began attracting comments in the financial press. Dome's scheme to get its hands on HBOG cash flow was not sufficient. Using 1980 as their frame of reference, Dome claimed that, with its own $450 million in cash flow plus the $301 million from HBOG[71] it could survive.

THE PITFALLS OF DOME'S ACCOUNTING METHODS

Analysts were beginning to publicize the full impact of Dome's accounting methods. Dome used 'full-cost accounting' which is acceptable under GAAP (Generally Accepted Accounting Principles). For Dome, full-cost accounting consisted of capitalizing exploration and interest costs over a period of years rather than expensing these costs immediately. The result of this method was to produce higher profits than under other costing methods. In a 1981 *Accounting Alerts Bulletin*, William Scott, an accountant with F.H. Deacon, Hodgson Inc. of Toronto noted that Dome uses 'full-cost' accounting and it capitalizes a large amount of its interest costs. This means that rather than reporting all its exploration expenses and interest costs in the year they take place, Dome deducts them from its income statement over a period of years. As a result, Dome is able to report a higher profit.[72] In 1981, Dunnery Best reported in the *Financial Post* that to service the interest payments on the new debt resulting from the HBOG purchase, Dome was paying approximately $387 million annually. The *Financial Post* reported that Pan Canadian Petroleum Limited, Husky Oil Limited, Ranger Oil, and Alberta Energy also used full-cost accounting.[73] In 1981 Dome actually expanded the practice. After 1980 exploration expense would encompass all costs of exploration.[74] It may be that Dome's financial problems induced it to adopt accounting measures which would present its cash-flow position in a more favourable light.

Some analysts adopted a highly critical attitude towards Dome's cash flow. Paul Joseph, an oil analyst at Burns Fry Limited, recommended selling Dome shares in May 1981. This recommendation was considered very controversial because Dome was trading at an all-time high of $25 per share.[75] Part of the Burns Fry strategy was to look closely at cash flow. Gwyer Moore at Burn's Fry said that '[C]ash flow is more meaningful because exploration outfits garner many writeoffs and because of the accounting practice of capitalizing interest payments'.[76]

Dome cuts back

After Dome completed the acquisition of HBOG in March 1982, rationalization became a necessity. In the same month Dome quit hiring new employees. By the middle of April, Dome had laid off 150 of its almost 10,000 employees.[77] Most Dome employees were in Western Canada. There are however, 2,300 employees in Quebec at the Davies Shipyard in Lauzon and about 500 employees in the United States.[78]

During 1982 Dome was busy selling off assets it had acquired with the HBOG purchase. Dome Canada, 43 per cent owned by Dome Petroleum, agreed to pay $460 million for a 12.5 per cent interest in HBOG's properties in Western Canada. A subsidiary of Dow Chemical agreed to pay $430 million for a 12.5 per cent stake in HBOG's western Canadian properties. TransCanada Pipelines, 47 per cent owned by Dome Petroleum, was considering buying a 12.5 per cent interest.[79] At the end of March 1982 Dome Petroleum had current assets of $2.2 billion and current liabilities of $3.4 billion. These current liabilities were comprised of $2.6 billion in debt repayment due within the year ($300 million was due in June).[80] By the end of March, Dome's bankers were involved again. A proposed sale of preferred stock had not come to fruition and Dome needed another $80 million to pay March bills. The bankers were reluctant but Richards talked to Marc Lalonde, Energy Minister, and Ottawa applied pressure on the banks.[81]

Dome employees were beginning to worry about the future. Employees who were not laid off were showing up in Calgary recruiting offices.[82] The *Toronto Star* reported on 19 June 1982 that the banks were now approaching Lalonde about Dome.

During the middle of June, because of their concern about a possible Dome bankruptcy, Dome Canada attempted to buy Canmar (Dome Petroleum's drilling fleet) for $200 million in an attempt to funnel money back into the parent company. The *Economist* reported that the federal government was sending conflicting signals regarding Dome. The government ordered Petro-Canada to guarantee $100 million loan to Dome Canada from the Toronto Dominion Bank, the Bank of Montreal, the Royal Bank, and the Canadian Imperial Bank of Commerce. The loan would finance 50 per cent of the purchase of Canmar.[83] The purpose of the loan was to provide bridge financing until Dome Canada received its first PIP grant. Ten days later the grants were received and the loan was repaid. The sale of Canmar was later cancelled because Canmar had

been pledged as security against a Dome Petroleum loan. The $100 million payment has since been changed to a loan from Dome Canada to Dome Petroleum.

In addition, the government revised regulations so that PIP payments could be received monthly, not quarterly. The reason given was that since exploration activity was so seasonal, it was too much to ask recipients to wait for three months. In fact it looked like yet another move to keep Dome afloat.[84]

By 30 June 1982 Dome's debt stood at $7.03 billion. This included $2.41 billion in long-term debt due within one year; $284.4 million in bank loans; $1.04 billion in accounts payable; the $100 million demand loan from Dome Canada; and $3.2 billion in long-term debt of various maturities.[85]

The political debate on Dome

On 7 September 1982 Prime Minister Trudeau was saying that Dome would not be bailed out because of the precedent it would set for other private firms. The federal government's initial reaction to Dome's difficulties was a response to the opposition parties' attitude towards Dome. Opposition MPs insisted that the government had already given Dome many indirect funds and a Dome bailout would be out of the question.[86]

On the other hand, other MPs were critical of the Liberals because of the adverse effect that the National Energy Program had upon Dome.[87] Jack Shields MP (Athabasca) noted that Western Canada did not want the NEP which was supposed to increase Canadian ownership of the oil industry; it had only increased the industry's difficulties. Don Mazankowski, a PC from Alberta, noted Dome's $7.8 billion debt and blamed it on the NEP which had lured Dome into takeovers.[88] During discussions with Conoco Chairman Ralph Bailey prior to the original HBOG purchase, Richards and Gallagher suggested that Conoco's interest in HBOG was worth less to the US company than it would be to Dome, since Canada's NEP severely hampered foreign-controlled oil companies operating in Canada.[89] The Liberal government had wanted to rely on private takeovers to 'Canadianize' the oil industry, and the policy had backfired. High interest rates and lower oil prices made the NEP's failure a certainty.[90] By June 1982 Allan MacEachen had asked Canadian

banks to reduce the number of new loans to finance oil-company takeovers and the banks had complied.

Dome's asset sale

By 19 June Dome's list of assets for sale included its US and Indonesian holdings, its North Sea holdings, and the Cyprus Anvil Mines. There was also talk of selling Dome Mines and TransCanada Pipelines. The Alberta government stated at this point that they would not assist Dome; it took the position that it had already done its part by reducing taxes and royalties. Alberta had entered into an elaborate pricing agreement with Ottawa in September 1981. The agreement was predicated upon high world prices. By 1982, Alberta was pressed to react to the industry's problems. Alberta also justified its refusal to assist Dome over others. Alberta subsidies favour small companies based on the argument that small firms are relatively more likely to expand employment and improve technology in the industry.[91] By putting a $4-million ceiling on the amount of royalty relief a company can take, the Alberta government favours the creation of many small firms in the oil-exploration industry.

In late June the popular press argued that Dome should not be allowed to fail. For example, a *Toronto Star* article on 25 June 1982 gave seven reasons:

1 The Canadian banks were heavily exposed in Dome.

2 There were 9,950 Dome employees, some of whom would lose their jobs.

3 Beaufort exploration and oil self-sufficiency would be undermined (the tar sands project was shelved during the year and northern oil was the only big oil frontier left in Canada). Dome was expected to spend $4 billion by 1986. PIP grants would foot 80 per cent of the bill, and Dome had the expertise to run the project.

4 Dome is Canada's largest producer of natural gas, and third-largest producer of oil.

5 Dome's extensive parts-supplier network, particularly in western provinces, would be hurt.

6 A number of oil companies shared millions of dollars in drilling commitments with Dome and a Dome failure might halt some of this drilling activity.

7 Dome had a high financial profile and the effect of a Dome collapse would have a negative impact on stocks and the money market (particularly short-term effects on the Canadian dollar).[92]

But no matter how speculative the effects of a Dome collapse, the prospect of a Dome collapse was becoming more likely. On 1 July 1982 with $300 million in principal due, Dome began paying only interest with no principal reduction.[93] Even good news did not convince shareholders. On 17 July the *Globe and Mail* reported that Dome had been awarded contracts for the Liquified Natural Gas project in British Columbia. The project would employ 120 people in the immediate future and 1,300 people at the peak of production. Share prices rose to $6 but then fell to $5.62. Although the Liquified Natural Gas project meant $100 billion in revenue over twenty years, investors were worried about the next five years.[94]

DOME'S DESPERATE ATTEMPTS TO RAISE CASH

On 15 July the sale of Canmar to Dome Canada fell through because the US consortium refused to let the deal go through. The consortium had a negative pledge on the fleet as part of the security for its HBOG loan.[95] On 24 July Dome reported: first, a 10 per cent pay cut for its workers to save $20 million per year; second, a benefit cut; third, a 15 per cent staff reduction at head office; fourth, the closing of its Halifax recruiting office; fifth, an increased work week of one hour and forty-five minutes; and sixth, no hiring of summer students. On 3 August, 25 per cent of US workers were laid off[96] (the US staff was mainly clerical).

As for other sources of cash, Dome announced on 9 August 1982 that it would sell its Indonesian holdings for $400 million.[97] On 11 August it was reported that Dome obtained only $340 million for its Indonesian holdings.[98] Meanwhile, Dome Petroleum shares were now selling for $3.85 versus a 1981 low of $11.25.

In a contemporaneous effort to raise cash, Dome offered to repurchase Dome Resources' preferred shares for $50 per share. If Dome Petroleum could acquire the Dome Resources' preferred shares, it was entitled to draw on the line of credit securing the shares. Because the Dome

Resources preferreds were trading between $48 and $49 per share, less than half the anticipated number of shares were tendered and Dome's effort to obtain additional US bank credit met with only limited success.

By now nervousness was reaching epidemic proportions. On 21 August Dome Petroleum's shares fell to $3 per share simply on rumours of bankruptcy in New York and rumours of interest moratoria in London. A Frankfurt lender had to be calmed on 12 September in order to avert an immediate bankruptcy.[99] Prime Minister Trudeau kept insisting that Dome and the banks would have to solve Dome's problems.[100] But the third week of September, the government and the banks presented Dome with the 'solution'.

THE BAILOUT

Bank involvement

Before discussing the terms of the bailout, it might be helpful to understand why the banks were so heavily involved in the negotiations. This is best understood by looking at the bank exposure in Dome Petroleum. By the third quarter of 1981, the *Financial Post* reported some statistics gathered by Hugh Brown, a banking analyst at Burns Fry. He estimated Canadian-dollar bank loans to the oil industry at $10 billion at that time. This compared to Bank of Canada figures of bank-dollar loans to the industry which were $5.7 billion in 1980, $3.1 billion in 1979, $1.8 billion in 1978. They reported that at the end of the first quarter of 1981, the Canadian dollar loans totalled $6.1 billion or 10 per cent of all Canadian-dollar business loans made by Canadian chartered banks.[101] In 1978, only 5 per cent of Canadian business loans were to the petroleum industry. The *Financial Post* reported that Canadian bankers were reacting to competition from foreign banks in anticipation of the new Canadian Bank Act.

The banks explained their reactions by stating that they did not anticipate the effects of the recession. Further, when the extent of the oil industry's problems became evident, the banks said they believed the oil companies had 'a couple of tough years to go through, but had long-term reserves'.[102] A *Financial Post* reporter stated that 'the Canadian banks have become partners with many of their energy clients, some of whom, in reality, are now working for their banker, and rather more remotely for their shareholders'. The stockholders in the banking community were not pleased. Bank analysts with F.H. Deacon, Hodgson Incor-

porated in Toronto pointed to 'the weight on energy lending as one of the factors holding back the market price of bank shares'.[103] Table 27 is a list of troubled oil companies and their financial characteristics to highlight the banking community's lending record.

Table 28 illustrates the exposure of the Big Four banks to Dome Petroleum. This total indebtedness at the end of 1982 was $3.145 billion dollars. At the height of the bank's exposure to Dome, which occurred between the original loan for HBOG and the disposition of HBOG assets to Dome's corporate family and friends, the total indebtedness of the Big Four was about $1 billion greater.[104]

The Bank of Nova Scotia, which was not involved in the original HBOG purchase, was involved with Dome through their loan of $350 million to HBOG for the purchase of Cyprus Anvil Mines. The mine was purchased for $340 million but valued only at $170 million by the summer of 1982.[105]

After having spent weeks in secret meetings together, the banks, the federal government and Dome Petroleum announced that the firm's existing debts would be rescheduled and fresh capital would be raised through a new debenture issue. The general terms of the proposed bailout are as follows:

1 The federal government and four Canadian banks (Canadian Imperial Bank of Commerce, Royal Bank of Canada, Bank of Montreal, and Toronto Dominion Bank) would provide $1 billion of new capital; $500 million would come from the federal government and $175 million from CIBC, $135 million from TD, $140 million from Bank of Montreal and $50 million from the Royal.[106]

2 These new debts would take the form of convertible debentures, half to Ottawa and half to the four banks.

3 The interest rate on the debentures would float at one percentage point above the prime rate, with interest to be paid in common shares instead of cash for the first two years.

4 An additional $500 million worth of identical convertible debentures would be offered to existing shareholders.

5 The debentures would be convertible to common shares at the following rates: $2.50 for the first eighteen months, $2.85 for the next year,

TABLE 27
Select financial characteristics of oil companies, 1982

Company	Debt (millions)	Funds from operations		Interest		Bank
Drummond	$ 34	$800	M (monthly)	$ 1.9	M (monthly)	–
Coseka Resources	143.6	15.8	M (yearly)	20	M (yearly)	Royal
Sulpetro	783	145	M (yearly)	135	M (yearly)	Royal
Czar	60	12	M	10	M	TD
United Cargo	191	21.9	M	32	M	CIBC
Turbo	600	40	M	90	M	CIBC
Brent Petroleum	77	25	M	27	M	CIBC

SOURCE: *Financial Post*, 10 April 1982.

$3.35 for the following year, $3.90 for the following year, $4.50 for the following year, and $5.00 for the last 18 months.

6 The banks agreed to reschedule Dome's outstanding debt (about $7 billion) by postponing its maturity for up to ten years.

In addition, the government would receive the right to buy the Beaufort operations at an independently established price if Dome failed to spend adequate amounts on northern exploration. The agreement stated that reasonable levels of expenditure on Beaufort exploration should be maintained and that failure to do so would trigger the government's buy-out option. Moreover, the government and the banks would have control over appointments to Dome Petroleum's board and the hiring of senior management. The veto power is shared fifty-fifty by the governments and the banks. The bank veto power is, in turn, divided proportionally among the banks based on the amount of money owed.

At the time of the proposed bailout Dome had 31,800 shareholders.[107] The terms of the proposal would substantially reduce these shareholders' claims on the company's assets and their earnings per share. The agreement would result in a substantial increase of shares outstanding. Almost 700 to 800 million shares would be in circulation if the government and the banks exercised their conversion privileges. The proposed bailout has had a disastrously adverse affect on Dome employees, many of whom are also Dome shareholders. One journalist reported that many Dome employees had moved to Calgary attracted by the boom-

TABLE 28

Canadian bank exposure to Dome, December 1982 ($ million)

Bank	Dome loan	Security		Dome loans as a percentage of assets	Dome loans as a percentage of capital
CIBC	$941.9	Dome Energy Ltd.	$260.1	$1.4	$39.6
		Musketeer	144.5		
		Dome investments:			
		TransCanada PipeLines	265.8		
		Dome Canada	165.0		
		Other	100.0		
		112572 Canada Inc.	5.5		
		Alerk	1.0		
Toronto Dominion	986.2	Dome Energy Ltd.	260.1	2.2	56.0
		Musketeer	216.0		
		Dome Oils Inc.	95.0		
		Cyprus Anvil	130.0		
		Canpar FRN's Dome	86.7		
		Canpar FRN's Provo	124.0		
		Canpar FRN's Provo	74.4		
Bank of Montreal	928.6	Dome Energy Ltd.	260.1	1.5	56.0
		Musketeer	144.5		
		Natural Gas Liquids Plant A	200.0		
		Natural Gas Liquids Plant B	124.0		
		Income Debentures	200.0		
Royal	287.8	Dome Energy Ltd.	260.1	0.3	10.0
		Goliad	2.5		
		Orion Bank Ltd.	25.3		

SOURCE: Foster, Peter (1983) *Other People's Money*, 276-7.

ing oil industry. These latecomers, many of whom had bought houses at the height of the real-estate market saw their house value and stock values plummet simultaneously.[108]

The primary negotiators for the government were Mickey Cohen,[109] Deputy Minister of Energy Mines and Resources, and Edmund Clark, the Senior Assistant Deputy Minister of Energy Mines and Resources, who was one of the architects of the National Energy Programme.[110] Dome Petroleum was a party to the bailout negotiations only after the principal bailout proposal had been developed by the government and the banks. Once involved, Dome was represented by Jack Gallagher, Bill Richards, and Terry Hargreaves, the manager of Dome's Ottawa office.

Stock market reaction

On 23 September 1982, a Dome official called the Toronto and American Stock Exchanges to halt trading of Dome shares pending the announcement of the proposed bailout. On that day, Dome shares were trading at $5 per share. During the week after the announcement, Dome stocks fell $1.88. During 1982, on the Toronto Stock Exchange, Dome prices went from a first-quarter 1982 high of $15 to a fourth-quarter 1982 low of $2.55. On the American Stock Exchange, they went from a first-quarter high of $12.63 to a fourth quarter low of $2.07. Table 29 illustrates Dome Petroleum stock performance before and after the bailout proposal. Some stock-market analysts described the bailout as 'Draconian'. The fully diluted number of shares (including conversion to common shares by the government, the banks and Dome shareholders) would mean almost 1 billion common shares outstanding. The analysts also argued that the proposed bailout would put a ceiling on Dome share values over the next seven years.[111]

In addition to Dome Petroleum's stock market performance, Dome's bankers and Dome's subsidiaries also suffered during the week after the bailout proposal was announced. Table 30 shows their stock performance for the week ending 2 October 1982. The Bank of Commerce, whose stock prices fell the most of all the subsidiaries and banks involved, has the highest exposure in Dome and other financially troubled companies (Massey Ferguson, Maislin, Turbo, etc.).

In December 1982 Dome shareholders reacted by forming the Dome Shareholder's Investment Committee to oppose the proposed bailout.[112] The Committee was organized to lobby for several key changes in the

TABLE 29
Market for Dome Petroleum's equity

	Toronto Stock Exchange (Canadian dollars)		American Stock Exchange (US dollars)	
	High	Low	High	Low
1982				
1st quarter	15.00	7.88	12.63	6.50
2nd quarter	11.25	4.95	9.25	3.80
3rd quarter	5.88	2.85	4.75	2.19
4th quarter	3.70	2.55	3.00	2.07
1983				
1st quarter	17.70	14.10	14.95	11.80
2nd quarter	25.38	17.50	21.25	14.70
3rd quarter	24.88	11.25	21.25	9.38
4th quarter	16.25	11.63	13.75	9.63

NOTE: The approximate number of registered holders of common shares as of 31 December 1982 was 43,204. The company has not paid dividends on its common shares since the Company's inception and there is no expectation it will do so in the near future. Per share amounts have been restated to reflect the five for one common share split effective 22 May 1981.
SOURCE: 1982 Financial statements of Dome Petroleum Ltd.

TABLE 30
Stock market performance, Dome and bankers (week ending 2 October 1982)

	Week's close in dollars	Week's change	1981 high
Dome Petroleum	$ 3.25	$ – 1.88	$25.38
Dome Mines	11.38	–.13	20.00
Dome Canada	4.50	–.50	11.50
TransCanada Pipelines	20.50	–.88	27.50
Bank of Commerce	21.50	– 1.00	32.13
Royal Bank	21.50	–.25	32.50
Bank of Montreal	20.88	–.13	33.50
Toronto Dominion Bank	30.00	–.25	35.50

SOURCE: *Toronto Star*, 2 October 1982.

refinancing package. In particular, they wanted the common share conversion price for the proposed debentures to be raised to more than the planned $2.50 per share. As well, the Committee wanted to prevent the banks and the government from converting the debentures into common shares for at least two years. The existence of the Committee was looked upon favourably by Dome Petroleum officials as an indication of shareholder support, and as a means of gauging market response to an equity sale as an alternative to the proposed bailout.[113]

The effect on TransCanada Pipelines

Subsequent to the bailout proposal, substantial proportions of its 47 per cent interest in TransCanada Pipelines have been sold by Dome Petroleum. In early February 1983 Dome Petroleum and Dome Canada announced that they planned to sell half of their combined stake in TransCanada.[114] Dome Petroleum reported that it received $146.8 million from the sale of TCPL.[115] On 12 July 1983 Dome Petroleum reported that it would sell its remaining shares in TransCanada. The 4.3 million common shares would be sold to three Toronto-based brokerage firms and would raise $120 million in additional cash. TransCanada executives were reported to be relieved. One executive was quoted as saying, 'Although TransCanada's health was never directly threatened by its close association with Dome, the fact that Dome owned such a large piece of TransCanada made it difficult for the utility to raise its own funds in the financial market'.[116]

The effect on Dome Canada

Dome Canada has also been adversely affected by its Dome affiliation. After the February TransCanada sale was proposed, a Dome Canada source reported 'that the banks would not provide additional loans for Dome Canada until the financial problems of its parent company, Dome Petroleum, are resolved'.[117] If the banks had not decided to tighten up on their loans, Dome Canada would probably have been able to keep its shares in TransCanada Pipelines.

The effect on Dome Mines

Dome Mines has also been constrained by its Dome Petroleum affiliation. Because of its 27 per cent ownership of Dome Petroleum, Dome Mines

could be a party to the proposed bailout. At the time of the announcement of the proposed bailout, Dome Mines guaranteed to a maximum of $250 million a bank loan made to Dome Energy Limited, a holding company of Dome Petroleum.[118] In addition to the debt guarantee, the Dome Mines equity holdings in Dome Petroleum have had a negative impact on Dome Mines' income statement. In 1982, Dome Mines had a profit from operation of $54.6 million but there were extraordinary losses: a net loss of $74.6 million or $1.07 per share.[119] Dome Petroleum's 1982 loss of $110 million contributed substantially to this disappointing performance by Dome Mines.

During the year, Dome Mines has also had to sell many of its assets. In a move during the year to gain funds and reduce debt, Dome Mines and its subsidiary Campbell Red Lake Mines Ltd. sold their combined 10 per cent holdings in Denison Mines for a gain of $17 million. It was also forced to sell its 25 per cent interest in the nearly completed Detour Lake Mines to its debt-free affiliate Campbell Red Lake Ltd. With respect to this move Dome Mines secretary, John Hick, said that 'The original idea was to hold on to 25 per cent of the mine, or we would have had Campbell Red Lake buy it in the first place'.[120] On 22 June 1983 Dome Mines announced another divestiture to reduce bank loans. Dome Mines sold its Noranda Mines shares for $30.3 million.[121]

The effect of the proposed AIP on Dome Petroleum

After the agreement-in-principle was arranged, the Liberal government continued their indirect support of Dome while awaiting foreign bank approval of the proposed bailout scheme. In November 1982, officials at Industry, Trade and Commerce agreed to give CN Marine $15 million if it would accept a ferry bid submitted by Davies Shipbuilding Ltd. For the $15 million, the government would receive shares in CN Marine, which is wholly owned by Canadian National Railways. In essence, Ottawa would buy new shares from a company it already owns to clinch a low-bid contract for a Dome subsidiary.[122] The government would also get a rollback by union workers from their 13 per cent wage settlement to the government's '6 and 5' scheme. The unions were reportedly cool to this. The government also agreed to provide assistance to Cyprus Anvil Mines. In April, the federal government approved a $50-million rescue package to the mining company. The package is for $25 million for each of the next two years, half from the government, and half from Dome

Petroleum. The Yukon government has also promised to contribute $2 million. The money will benefit the Yukon since Cyprus Anvil revenue represents 40 per cent of the Yukon's total GPP. The financing should also make the mine more attractive and it is no secret that the federal government would like Dome to sell the mine.

In an effort to placate the banks, Dome made some managerial changes. On 8 April 1983, Jack Gallagher resigned as Chairman of Dome Petroleum. Regarding Gallagher's departure, a Dome director said, 'It wasn't direct pressure but there's no question the banks have been concerned about whether management that got the company into all this debt could get it out of that situation.'[123] His departure was followed by the resignation of Bill Richard in September 1983.

Gallagher's successor, Howard MacDonald has devoted much of his efforts to cleaning up the Dome balance sheet and finalizing the rescheduling of Dome debt with the banks involved (see Table 31 for a list of Dome lenders as of 31 December 1982). Part of this effort to improve Dome's balance sheets has been targeted toward reducing Dome debt by selling off assets. In March 1983, Dome Petroleum reported that its September 1982 debt of $7.1 billion had been reduced to $6.5 billion. (Of this $6.5 billion, $3.76 billion is due to the Citibank consortium and $1 billion is due to unsecured creditors.[124]) Ten months later, MacDonald had reported a $5.3 billion debt load. Mr. MacDonald said that the divestiture of 'non-core businesses' such as Sovereign Oil & Gas (which was sold to Home Oil Co.) have allowed Dome to wipe out $1 billion in debt. Further asset sales also are being negotiated – including Davies Shipbuilding Ltd., the Les Mines Selbaie copper, silver and gold mines and the Cyprus Anvil Mining Corp. zinc mine.[125] Cleaning up the balance sheet has also resulted from the writedown of assets. In their 1983 financial statements, Dome management reported a $1.1 billion loss. The biggest proportion of the loss was attributable to a writedown of noncash generating assets worth $897 million.

Howard MacDonald's task of arranging the rescheduling was prolonged. The diversity of each banks' security created an atmosphere for strategic behaviour. The *Financial Post* reported that the US banks with unsecured exposure might be willing to participate, but there was no incentive for many banks in the consortium to take on an additional $500 million in debt.[126] The Citibank consortium set up a $400 million collateral account when the original 1.7 billion loan was arranged with Dome Petroleum. (Such collateral accounts are fairly common in the banking

TABLE 31
List of Dome's lenders and amounts of loan

Dome's lenders	Outstanding principal as at 31 Dec. 1982 ($ million)
Canadian Imperial Bank of Commerce	$941.9
Toronto Dominion Bank	986.2
Bank of Montreal	928.6
Royal Bank of Canada	287.8
Crédit Agricole	84.4
First Interstate Bank of California	84.4
The First National Bank of Chicago	84.4
International Westminster Bank Ltd.	84.4
Manufacturers Hanover Trust Co.	84.4
Morgan Bank of Canada	84.4
NBC	84.4
Security Pacific National Bank	63.3
Marine Midland Bank, N.A.	42.2
National Bank of Detroit	42.2
Bank of British Columbia	21.1
The Bank of New York	21.1
Continental Bank of Canada	21.1
European American Banking Corp.	21.1
The Fuji Bank Ltd.	21.1
The Industrial Bank of Japan, Ltd.	21.1
Security Pacific Bank Canada	21.1
The Sumitomo Bank, Ltd.	21.1
Crédit Suisse	117.2
Citibank	194.0
Bank of America National Trust & Savings Assoc.	89.4
Chase Manhattan	109.7
Chemical Bank	94.4
Continental Illinois	214.2
Midland Bank	77.4
Crédit Lyonnais	96.4
Société Générale	71.4
Bank of Tokyo	21.1
Banque Nationale de Paris	35.3
Barclays	45.3
LBI (Canada) Ltd.	35.3
Treasury Branch-Musketeer Kaiser	29.7
Berliner Handel Sund Frankfurter	12.7
Deutsche Bank	25.3
Dresdner Bank AG	25.3

TABLE 31 (continued)

Dome's lenders	Outstanding principal as at 31 Dec. 1982 ($ million)
The Long Term Credit Bank of Japan, Ltd.	12.7
Swiss Bank Corp.	59.1
H.M. the Queen in Right of the Province of Alberta	10.0
Canada Permanent Trust Co.	50.0
Canada Trust Co.	25.0
Royal Trust Corp. of Canada	18.0
National Trust Co. Ltd.	5.0
Saskatchewan Co-Operative Credit Society Ltd.	5.0
The Mutual Life Assurance Co. of Canada	2.0
Marubeni	107.0
10.5% Prudential Debentures	175.2
Arctic Petroleum Corp.	175.0
Lynco Notes	6.1
1st Mortgage Rev. Bonds	3.7
Public bonds, debentures, etc.	611.6
Other and foreign exchange	94.2
TOTAL	6,705.5

SOURCE: Foster, Peter (1983) *Other People's Money.*

industry.) The existence of this collateral account, along with the fact that the consortium banks are fully secured, reduced the pressure on the consortium to go along with the bailout.[127]

The Liberals assisted Dome during the summer rescheduling negotiations by clarifying the government position on taxes and grants. In July the *Globe and Mail* reported that 'HBOG's highly profitable operations had been integrated with Dome, but there has been a problem in consolidating the two companies for tax purposes. In early July, the Finance Department ruled that the two companies could be consolidated for tax purposes and Dome was freed of its $315 million tax bill dating back to 1982. One Finance Department official reported that Dome was not getting special treatment and that any company in the same position would receive a similar ruling. The official also said that the Finance Department had decided to clarify its position on Dome so the company 'could proceed with its debt restructuring plan and the sale of shares to the public.'[128] In addition, the Alberta government has also agreed to a

measure of tax relief for Dome. The combined federal and provincial tax deferment is close to the $379 million owed by Dome in September 1984. Subsequently, the federal government announced on 8 February 1985 that the federal government had also given Dome a four year extension – from January 1985 to January 1990 – for payment of $199 million owed in petroleum and gas revenue taxes.[129]

In addition, Ottawa relaxed its Canadian Ownership Rules in August. This ruling assisted Dome's proposed equity sale. Dome promised in 1981 that it would become 50 per cent Canadian and thereby meet the guidelines for Ottawa's National Energy Program. Regrading the COR ruling, one Dome spokesman stated: 'we have a letter from the federal government saying that they fully understand our situation and will not hold us to commitments to Canadianize the company.' A Calgary analyst reported that with the proposed equity sale Dome could wind up with 80 per cent non-Canadian ownership.[130]

On 5 February 1985 Dome's lenders agreed to extend principal repayments on $5.3 billion, or 83 per cent of Dome's debt, over twelve years and to drop a requirement for an immediate $350 million share issue that had been part of a prior rescheduling proposal arranged in August 1984. However, Dome has agreed with its lenders to raise $100 million by 31 December 1986 through the sale of common shares or other securities approved by the lenders. The new debt rescheduling agreement results in repayments of $3.6 billion until 1988. The lenders will receive interest rate increases of one-eighth of one per cent annually effective 1 April 1984. The agreement also provides Dome with $245 million in operating credit secured by accounts receivable.[131]

But Dome chairman Howard MacDonald stated that the risks for Dome Pete are still there.[132] Dome is plagued by uncertainties relating to interest rates, oil prices and the value of the Canadian dollar. MacDonald stated in December that each percentage point drop in interest rates translates into $53 million of added cash flow. But this scenario looks good for Dome only in a world of falling interest rates. Mr. MacDonald also stated that each $1 a barrel increase in the price of oil results in $18 million of added cash flow and that each increase of $10 million cubic feet a day of gas translates into an added $5 million of cash flow per year.[133] On 6 February 1985 Dome reported that regarding profit (not cash flow), each percentage point change in interest rates changes its profit by $27 million and a $1 change in oil prices changes profits by $8 million.[134] To protect itself against the kind of upside swing

in interest rates, Dome will convert up to half of its debt into fixed-rate debt.[135] In addition, the rise and fall in the Canadian dollar has a substantial impact on Dome's financial performance since 60 per cent of Dome debt is in U.S. dollars.[136] In 1983, Dome had a $72.3 million foreign exchange loss resulting from the fall in the Canadian dollar.[137] The *Globe and Mail* reported on 6 February that the rescheduling could improve Dome's 1984 financial statement in that a reduction of debt currently payable cuts the size of foreign-exchange losses.[138]

Finance Minister Michael Wilson announced in the fall of 1984 that the new Tory government would not renew the bailout agreement. For Dome the agreement in principal was a staying action while the company was able to get the banks to agree on a rescheduling of debt. Dome Petroleum and the banks are still very uncertain about the future of their investments.

NOTES

1 Foster, Peter (1983) *Other People's Money* (Toronto: Collins) 33.
2 Foster, Peter (1982) *The Sorcerer's Apprentice* (Toronto: Collins) 58-59.
3 Ibid., 150.
4 Francis, Diane, (1983) 'What made Taschereau quit'. *Toronto Star* 31 May.
5 *Oil and Gas Journal* 1 December 1980, 92. In fact, the Beaufort testing has yet to prove its value commercially. Richards protected himself from this lack of hard data by explaining that one year of normal drilling is equivalent to five years of drilling in the Beaufort.
6 *Fortune*, 11 August 1980.
7 *Saturday Night*, July 1982, 13.
8 Foster (1982) op. cit., 215.
9 1979 – 1980, 10K. report to the US Securities and Exchange Commission.
10 *Fortune*, 11 August 1980.
11 Foster (1983) op. cit., 56.
12 Foster (1982) op. cit., 221.
13 *Montreal Gazette*, 8 June 1981.
14 *Saturday Night*, July 1982, 13.

15 TransCanada Pipeline is the conduit used to transport natural gas from Alberta to the Eastern Canada and US markets.

16 Dome Mines also has a 25 per cent interest in Dome Petroleum outstanding shares and therefore is its principal shareholder.

17 Siebens Oil and Gas has a 30 per cent interest in Siebens UK. Siebens UK, in turn, has substantial holdings in the North Sea including a 4 per cent interest in the Brae fields.

18 As Dome points out in its financial statements, deferred taxes are generally not a problem as long as the company's capitalized asset base (CCA) is growing. The asset values of resource industries increase as the price of the resources increase.

19 Foster (1983) op. cit., 89.

20 Tax and royalty relief would come later as the industry began suffering from decreased oil prices. Alberta reduced taxes in April 1982 and the feds in May 1982.

21 Foster (1982) op. cit., 217.

22 Lyon, Jim (1983) *Dome: The Rise and Fall of the House that Jack Built* (Toronto: MacMillan) 7.

23 Foster (1982) op. cit., 217.

24 *Financial Post*, 7 February 1981.

25 Lyon (1983) op. cit., 10-11.

26 Best, Dunnery (1981) *Financial Post*, 31 October.

27 Foster (1983) op. cit., 97.

28 Foster (1982) op. cit., 158.

29 *Macleans*, 31 May 1982.

30 Government figures of 35 per cent Canadian content would mean 67.75 per cent; the new issue contribution of 52 per cent plus the Dome Petroleum Canadian contribution (3.5% x 45% of 15.75%).

31 *Financial Post*, 17 January 1981.

32 *Hansard*, 18 May 1982.

33 Foster (1982) op. cit., 213.

34 *Toronto Star*, 28 July 1981.

35 Best, Dunnery (1982) 'Horn River metamorphosed into Dome Resources'. *Financial Post*, 1 May.

36 Taylor, Paul (1981) 'Rising debt may become issue for Dome Management'. *Globe and Mail*, 16 September.

37 Evans, Eric (1981) 'Dome tiptoes through a mine-field of debt'. *Financial Post*, 5 September.

38 *Financial Post*, 25 July 1981.

39 *Canadian National Journal of Business Investment and Public Affairs*, 4 June 1981.

40 *Financial Post*, 16 May 1981. In the House of Commons, Dome's tax avoidance was discussed. Ian Waddell noted on 13 May 1982 that Dome does not pay taxes and this is a difficult matter to explain to constituents.

41 Evans (1981) op. cit.

42 *Toronto Star* (1983) 'Magazine ranks Dome as leading gas producer', 7 June, p. C3.

43 *Financial Post*, 25 July 1981.

44 Several other Canadian purchases were occurring at this time. The most notable one was the purchase of Cities Service Company by the Nu-West Group. Here again, the allegations were:

1 That the lack of legal restrictions on bank investment policies enabled Canadian companies to raise the necessary capital (in this case, the Toronto Dominion Bank put up $249.5 million).
2 They then bought US shares and converted these to Canadian shares at a distressed price. The US critics stated that Canadian tax laws gave Canadian advantage over non-Canadians and therefore the rate of return for US companies operating in Canada is lower and results in lower sale price of Canadian assets.
3 That necessary SEC filings were not made.

45 *Oil and Gas Journal*, 1 June 1981, 60.

46 Ibid.

47 *Globe and Mail*, 3 June 1981.

48 *Montreal Gazette*, 8 June 1981

49 Best, Dunnery (1981) op. cit.

50 *Financial Post* 20 June (1981)

51 *Forbes*, 12 October 1981.

52 *Montreal Gazette*, 10 August 1981.

53 *Globe and Mail*, 26 May 1983.

54 *Economist*, 3 July 1982.

55 Foster (1983) op. cit., 138; Foster (1982) op. cit., 128, 150.

56 *Globe and Mail*, 19 September 1981.

57 Best, Dunnery (1981) *Financial Post*, 31 October.

58 Evans, Eric (1981) op. cit.

59 *Calgary Herald*, 29 September 1981.

60 *Globe and Mail*, 16 September 1981.

61 Ibid., 1981.
62 Best, Dunnery (1982) *Financial Post*, 1 May.
63 *Globe and Mail*, 9 January 1982.
64 Tully, Shawn (1983) 'How Dome Petroleum got crushed'. *Fortune*, 10 January.
65 *Fortune* (1980) 'Prudhoe Bay is easier to interpret because its wells are on land or in shallow water', 11 August.
66 *Financial Post*, 9 November 1981.
67 Foster (1982) op. cit., 217.
68 Walkom, Thomas (1981) 'Return of tax breaks allows Dome to proceed with HBOG share bid'. *Globe and Mail*, 19 November.
69 These holdings were given as collateral when Dome purchased the original 53 per cent interest in HBOG.
70 The US banks claim that they were never notified of this change in terms.
71 Taylor (1981) op. cit.
72 Ibid.
73 Evans (1981) op. cit.
74 Dome petroleum financial statements, 1980.
75 Francis, Diane (1982) 'Paul Joseph saw Dome coming'. *Toronto Star*, 23 October.
76 Burns Fry issued buy orders for fourteen oil companies which have impressively outperformed the index as a whole. On average, the shares of these fourteen companies have leaped 42.8 per cent . . . the index as a whole by 16 per cent.
77 *Globe and Mail*, 15 April 1982.
78 Francis, Diane (1982) *Toronto Star* 25 July.
79 Taylor, Paul (1981) *Globe and Mail*, 23 November.
80 *Economist*, 3 July 1982.
81 *Fortune*, 10 January 1983.
82 *Toronto Star*, 8 June 1982.
83 Francis, Diane (1982) 'Would banks pull the plug if Dome fails to pay its debt'. *Toronto Star*, 25 June.
84 Lyon (1983) op. cit., 181.
85 Ibid.
86 *Globe and Mail*, 18 June 1982.
87 *Hansard*, 13 May 1982.
88 *Hansard*, 7-8 June 1982.
89 Lyon (1983) op. cit., 14.

90 *Hansard*, 8 June 1982, Ian Waddell.
91 *Toronto Star*, 19 June 1982.
92 Francis, Diane (1982) *Toronto Star* op. cit., 23 October.
93 *Economist*, 3 July 1982, 66.
94 *Globe and Mail*, 17 July 1982.
95 *Globe and Mail*, 15 July 1982.
96 *Globe and Mail*, 23 July, 3 August 1982.
97 *Financial Times*, 9 August 1982.
98 *Globe and Mail*, 11 August 1982.
99 *Toronto Star*, 12 September 1982.
100 *Globe and Mail*, 8 September 1982.
101 Evans, Eric (1981) 'Some takeovers just don't make sense'. *Financial Post*, 1 August.
102 Best, Dunnery (1982) 'Debt hazards plague the oil'. *Financial Post*, 10 April.
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14
The Atlantic fisheries

BACKGROUND

The Atlantic fishing industry has faced problems for decades. Traditionally, the policy response has been a series of royal commissions which enumerated the troubles, but did little to address them. However, 1981 was a particularly disastrous year for the Atlantic fishery and elicited a new approach. The industry had excess capacity and was inefficient, a situation caused in large part by Canada's 1977 declaration of a 200-mile offshore economic zone. The optimism this caused masked the severe structural problems the industry faced. From 1977 to 1981 the number of licensed fishermen increased by 45 per cent,[1] and the number of processing facilities increased by 35 per cent.[2] The industry was inadequately organized to deal with the expansion, and instead of acquiring new life, became overcapitalized and debt-ridden. Processing plants carry, on average, an inadequate equity base of 10 per cent. Fishermen had also increased their debt loads, the effect of which has been aggravated by high interest rates and escalating operating costs.

The industry faces a number of difficulties such as the inconsistency of product quality. Atlantic fish products have been forced into the middle-quality, moderately price-sensitive, 'value-for-money' market.[3] In this market, profits for producers depend on low production costs; difficult with producers in an over-extended, over-capitalized state. Due to the common property nature of the quota system, fishermen rush to bring in their catch early in the summer to make sure that they will receive their quotas.[4] This overloads the processing plants and often leads to waste. It also means that the plants which process the catch of the inshore

(seasonal) fishermen must shut down for six months of the year when no fish are being caught. A seasonal plant is inefficient and costly to operate.

Canadian producers are also overly dependent on one market. Eighty per cent of Canadian fish products are exported. Of these exports 52 per cent are sold to the United States, 10 per cent each to European markets and Japan, and 8 per cent to other markets.[5] The domestic market for fish is exceedingly weak.

The severity of the Atlantic fish industry's troubles became apparent in mid-1981 with the temporary closure of a number of large fish plants including one owned by Fishery Products Ltd. (FPL) at St. Anthony, Newfoundland. FPL is one of the 'big four' fish companies[6] of Atlantic Canada: the Lake Group Limited of Newfoundland, H.B. Nickerson and Sons Ltd. of Nova Scotia and Newfoundland, and National Sea Products of Nova Scotia (Nickerson-owned, but independently operated). At this point only National Sea, a more diversified company and the only one with publicly available financial statements, was operating at a profit (see Appendix I). A Woods Gordon study tracked 100 companies in the Atlantic fishing industry over a five-year period which included both their worst year, 1981, and their best year, 1978. In 1978 the companies showed profits of $29 million on sales of $642 million. By 1981, sales were up to $940 million but the companies lost $57 million. At this point only 27.5 per cent of the plants were profitable. During this period shareholders' equity fell from over $100 million to $26 million and working capital fell from $37 million to a deficit of $106 million.

A similar picture emerges for National Sea Products Limited (see Table 32). The company appears to have serious liquidity problems; the current ratio is just above unity and the quick ratio is very low and declining over the period 1980 to 1983. The problems caused by substantial use of debt are seen in the very low (negative in 1983) coverage ratios and high and increasing leverage ratios over the period.

The very low and negative return on assets (Dupont ROA) appears to be dominated by very poor profitability (as measured by net income divided by sales) since the turnover ratio (sales divided by average assets) improves over the period. The final financial indicator is the Z-score which in this case indicates bankruptcy for all years in the sample.

TABLE 32
National Sea Products financial analysis

	1983[a]	1982[b]	1981[c]	1980[d]
1 Current ratio	1.10	1.16	1.01	1.14
2 Quick ratio	.34	.34	.38	.43
3 Z score	(.74)	(.50)	(.43)	(.35)
4 Coverage ratio	(.07)	1.04	.73	.99
5 (EBIT)/average total assets	(.01)	.09	.07	.06
6 Net income/sales	(.04)	.003	(.003)	.01
7 Sales/Average total assets	1.61	1.54	1.49	1.41
8 (7)(8) = Dupont ROA	(.06)	.01	(.004)	.01
Leverage:				
9 Debt/(common + preferred)	4.67	2.43	1.64	1.50
10 (Debt + preferred)/common	5.16	2.60	1.77	1.62

a Year-end 31 December 1983.
b Year-end 1 January 1983.
c Year-end 2 January 1982.
d Year-end 3 January 1981.
Definitions:
Current ratio ≡ current assets/current liabilities.
Quick ratio ≡ (current assets – inventories)/current liabilities.
EBIT ≡ earnings before interest and taxes.
Coverage ≡ EBIT/(fixed charges).
SOURCE: Derived from financial information presented in *The Financial Post Corporate Service.*

In January 1982 in response to this crisis, Prime Minister Trudeau exercised the federal control over fisheries and commissioned a task force on the Atlantic fisheries. Trudeau appointed as chairperson Michael Kirby, former cabinet secretary for federal-provincial relations. He was given the mandate 'to recommend how to achieve and maintain a viable Atlantic fishing industry, with due consideration for the overall economic and social development of the provinces.'[7] Kirby was also to prepare policies that would ensure the long term viability of the industry without future infusions of public funds. According to Kirby, the objective of economic viability was to supersede the former objective of employment maximization.

Traditionally, the economic or commercial efficiency of the fishery and social, or maximum-employment, visions have conflicted. The fishery is vital to the 25 per cent of the total population of Atlantic Canada that

lives in fishing communities. Half of these communities are essentially single-sector economies with fishing and processing activity employing over 30 per cent of the labour force.[8] Therefore, although the industry supplies less than 1 per cent of Canada's GNP,[9] it is of vital significance to the Atlantic provinces.

ECONOMIC VERSUS SOCIAL VISIONS – THE POLITICAL DEBATE

The federal and Newfoundland governments repeatedly have used various policy instruments which have emphasized the social function of the fishery. In December 1981 the federal Department of Fisheries provided $13 million in loan guarantees to the Lake Group Ltd. of Newfoundland.[10] These were to expire 31 December 1982, but were extended until 31 December 1983 while the Kirby recommendations were considered. Assistance was given to protect the jobs of 2,500 workers employed in Lake Group's plants, the 1,600 fishermen, and the 29,000 people in fish-plant communities who, it was estimated, would be affected indirectly by Lake Group's failure.[11] From 1981 to mid-1982 the Newfoundland Department of Fisheries had provided over $27 million, largely in loan guarantees, to bail out thirty-one fish companies operating thirty-eight plants. The stated rationale was the saving of 7,000 jobs.[12] Invariably, the conditions set were the improvement of management, efficiency, quality, and marketing; performance of these conditions was weakly monitored.

In June 1982 the federal government leased the St. Anthony plant from Fishery Products Ltd., and operated the plant on a one-year basis as a Crown corporation. It was not certain that the St. Anthony plant would open for the 1982 fishing season because of financial problems. The delay would have left Atlantic Canada without its largest seasonal fish plant. On 11 June 1982 the federal cabinet approved three orders-in-council. The first stated that Fisheries Minister Romeo LeBlanc and two of his officials were to acquire all shares of St. Anthony Fisheries Ltd. (to be created from what was a plant of Fishery Products Ltd.) and hold them until 31 December 1982, thus formally making it a Crown corporation. St. Anthony Fisheries Ltd. had been incorporated in St. John's on 21 May 1982 by a lawyer acting for the federal government.[13] One week later the St. Anthony plant had re-opened. Under the second order-in-council, three fisheries officials were placed on the company's board of directors. Under the third, $8 million in loan guarantees were provided to the new

company through the Enterprise Development Program of the Department of Industry, Trade and Commerce.[14] Conditions were established for repayable contributions of $2 million. The government had acted to save 900 jobs at the St. Anthony plant, and to ensure that fishermen in the region had a plant that could process their catch.

The Kirby Report

With the public release of the Kirby Report in December 1982 (see Appendix 14-1), the two governments (Ottawa and St. John's) decided to change their approach to the industry. Rejecting the bailout instrument as excessively short term,[15] both governments decided to use the failing firms as a lever to restructure the industry. However, there was little agreement on how to approach the restructuring. Brian Peckford, premier of Newfoundland, reasserted the social function of the fishery when he stated, 'If the federal government decides to solve the fisheries problem on the basis of "raw economics" then Newfoundland might as well close up shop and steal away.'[16] The Kirby Report had recommended that a number of fish plants be closed. The Kirby Task Force (which was then transformed into the federal negotiating team on restructuring) recommended that plants at Burin, Grand Bank and St. Lawrence be closed. It also recommended that Gaultois, Harbour Breton and Rameal remain open for social reasons. These conclusions followed a study by Woods Gordon (commissioned by the task force) which found that, in 1981, twenty-six of the hundred companies surveyed had profits totalling $6.2 million. However, seventy companies (accounting for 83 per cent of the total sales of the companies surveyed) had lost a total of $64 million.[17] Peckford and James Morgan, Newfoundland's fisheries minister, rejected the idea of plant closure although Newfoundland was in agreement with the task force's recommendations concerning management, processing, and marketing in the industry.

Richard Cashin, head of the Newfoundland Fishermen, Food and Allied Workers Union proposed that the offshore trawler fleet, then owned by several companies, be amalgamated into a super-company with ownership controlled by the federal and provincial governments, banks, and the Newfoundland Fishermen, Food and Allied Workers (NFFAW) union. The current owners would be excluded since most were technically bankrupt. Cashin asserted that his 30 March 1983 proposal addressed the fundamental problems of the fishery and did not restrict

itself to the financial plight of the companies, which he believed was the main focus of the Kirby Report.

In April 1983 Donald Johnston, economic development minister, announced that Michael Kirby had been given instructions to negotiate a restructuring of the fish companies on the east coast. He was to discuss proposals with Newfoundland and Nova Scotia, the companies, fishermen, and the banks. Kirby was to report to the ad hoc committee of ministers on Atlantic fisheries restructuring (chaired by Johnston), as well as to Fisheries Minister Pierre De Bané. Johnston stated that to this point 'debate among ministers has centred on whether to spend millions simply bailing out the companies or to take shares in them.'[18] The idea then being negotiated, and one which was supported by Kirby, was an adaptation of Cashin's proposal. A major fish company would be created by pulling together the Lake Group with Fishery Products Ltd. (FPL) and several smaller firms in Newfoundland, and another would be formed by combining H.B. Nickerson with Nickerson-owned National Sea Products Ltd. in Nova Scotia. Newfoundland and the NFFAW opposed the plan since it was feared that a combination of Nickerson and National Sea would overwhelm the Newfoundland company in the marketplace. Nova Scotia, in turn, did not want to be blocked from the growth area of the rich cod fishery.

Unilateral restructuring

On 4 July 1983 the negotiations ended and Ottawa acted unilaterally to restructure the offshore fishery of Newfoundland.[19] One company would be created from Lake Group Ltd., Fishery Products Ltd., and John Penney and Sons Ltd., which were bankrupt.[20] Seventy-five million dollars was allocated by Ottawa as initial funding, while the companies' major creditor – the Bank of Nova Scotia – agreed to write off a proportion of the debt and take an equity position of $80 million. De Bané announced (with excessive optimism) that the plan would save 16,000 jobs. Ottawa would be the majority shareholder with the participation of the Bank of Nova Scotia, the Canada Development Corporation (with its 40.8 per cent share in FPL), and other private interests. De Bané stated that he could no longer negotiate with Peckford who had repeatedly introduced new demands despite agreements signed by James Morgan, Newfoundland's fisheries minister.

With this announcement federal-provincial conflict escalated dramatically. Although both governments had agreed on the restructuring objective, their visions of the industry differed. Newfoundland felt intense pressure to prop up fish-dependent communities. While Ottawa felt the same pressure, the Department of Fisheries was intent on reducing the overcapacity in the industry which Kirby had pinpointed as a major structural problem.

According to De Bané, Morgan had agreed to a compromise with the federal vision. On 18 May it was agreed that 'regarding plant rationalization the operations at Burin [would] be merged with Maystown, and operations at Grand Bank [would] be merged with Fortune while St. Lawrence [would] remain closed.'[21] They also agreed that redundant workers would not receive one year's severance pay (as had been stipulated in an earlier agreement) and that management of the new company would decide whether Burin and Grand Bank should close permanently. This last provision had been an amendment proposed by Newfoundland. Lake Group Ltd., John Penney and Sons, and FPL would be merged. Ottawa would put up all the required new capital and convert into equity its $13 million loan to the Lake Group. Newfoundland would convert into equity all its loans to the three companies.

The Newfoundland reaction

Morgan denied that Newfoundland had finalized the agreements and stated that those he signed remained subject to approval by the Newfoundland cabinet. The main problem remained: the fate of processing plants at Burin, Grand Bank, and St. Lawrence was undecided. De Bané (who asserted that he had Morgan's agreement) wanted them closed because it would cost $50 million over five years to support.[22] Newfoundland (Peckford) insisted they remain open to preserve jobs. De Bané believed that employment for those laid off at Burin and Grand Bank would be available at the more modern plants of Marystown and Fortune, ten minutes away.

On 30 June 1983 Premier Peckford went to the press and stated that throughout the negotiations, Newfoundland had 'stuck vigorously to [the] objective of an "all-plants open" policy.' He said Ottawa is 'proposing that the future of Grand Bank and Burin should be decided upon by management, [which would be] their death knell.'[23] It became evident that either Morgan had negotiated in bad faith by agreeing to

close St. Lawrence and by specifically requesting that management decide the fate of Burin and Grand Bank, or Peckford was changing Newfoundland's position in a desire to escape political responsibility for any plant closures. In frustration, the federal cabinet authorized De Bané to act unilaterally, which he did on 4 July 1983 with his announcement of a federal plan to restructure the fisheries.

Although DeBané made public his intention to restructure the industry, little appeared to happen immediately, in part because no group in Newfoundland would support his plan, and the federal government sought provincial approval for practical and political reasons. On August 26 1983 the Bank of Nova Scotia called $67 million in loans to FPL and placed the Lake Group Ltd. into receivership.[24] John Penney and Sons had entered receivership voluntarily on 25 August. The bank stated that it could wait no longer for a federal plan to save the companies. Federal negotiations with shareholders of these companies had reached an impasse. Shareholders, whose shares in companies with a negative net worth should have been worthless, recognized their leverage in a situation in which the federal government wished to prevent bankruptcy, but needed a shareholder agreement to do so. The receivers, Clarkson Co. Ltd., continued to operate Fishery Products Ltd. and the Lake Group. FPL Inc. and Caribou Fisheries Ltd., the companies' US marketing arms, remained out of the bank's control. Peckford immediately stated that Newfoundland intended to make a tender-offer for FPL and the Lake Group.

Ottawa's restructuring plan had stalled because FPL, controlled by its largest shareholder, the Canada Development Corporation (whose largest single shareholder is the federal government[25]), had failed to approve the plan – in part because CDC wanted $32 million more for its assets than Ottawa was willing to pay. On 30 August 1983 FPL asked the Newfoundland Supreme Court to force the Bank of Nova Scotia and the federal fisheries negotiation team to reveal any agreement not previously made public that related to the transfer of the firm's assets to a new federally backed company.[26] The new company was to have been the key instrument for restructuring the bankrupt fish-processing industry. FPL filed suit alleging that the bank unreasonably foreclosed on the company on 27 August – the day after federal-CDC negotiations to transfer FPL's assets fell through – in order to recoup $67 million in outstanding loans.[27] FPL alleged that the bank and Ottawa conspired to take possession of FPL's assets and turn them over to a new company, and

conspired to form an unlawful merger with Lake Group Ltd. and John Penney and Sons Ltd.

At this point FPL, its major shareholders, the government of Newfoundland, and the NFFAW were all opposed to Ottawa's plan[28] of 4 July. J.F. Collins, minister of finance for Newfoundland, termed De Bané's initiative 'a naked intrusion into an area of provincial constitutional jurisdiction, which is intolerable for any province . . . and the means by which its implementation is now planned is by a "secret agreement" engineering the seizure of privately-owned assets on the part of the bank and the federal government'.[29] He concluded that a 'super-company fishing industry, in which a distant federal government will have overwhelming ownership, bears the seeds of its own destruction, and that of the welfare of many families and communities dependent on it.'

On 25 September 1983 the Newfoundland Supreme Court rejected FPL's charges of conspiracy. Justice Gerald Lang stated that he found the charge to be 'absolutely ridiculous.'[30] At this point hearings were proceeding on the Bank of Nova Scotia's claims that the assets of FPLs marketing subsidiaries in the US and Europe were fraudulently transferred to another corporate entity to keep them out of reach of the bank.[31] On 14 June 1983 FPL's ownership structure had changed such that its Massachusetts-based marketing arm, F.P. Inc. fell within the jurisdiction of the US courts. Shares of F.P. Inc. were transferred to a numbered company, 123570 Canada Inc., which was 49 per cent owned by Monroe interests (FPL president Dennis Monroe), 49 per cent owned by CDC (48 per cent owned by Ottawa), and 2 per cent to Harold Earle, FPLs chief financial officer.[32] Monroe defended the move by stating that FPL had wanted to avoid restructuring when it was turning itself around financially.[33] It had had three years of heavy losses, but had made a net profit of $1.4 million in the first six months of 1983. It had also reduced its loans from the Bank of Nova Scotia to $68 million from the 1982 level of $82 million. This trend to profitability made the bank's decision to appoint a receiver highly suspect in the view of FPL officials.

The CDC-FPL suit against Ottawa, the Bank of Nova Scotia and Michael Kirby was dropped during appeal proceedings. The bank's suit against the FPL and the CDC, alleging fraudulent transfer of assets to a numbered company, was also dropped.

Newfoundland

On 26 September 1983 Ottawa and St. John's completed an agreement on restructuring the province's deep-sea fishing industry.[34] The two governments became shareholders in a new company formed from the Canadian and American assets of FPL, the Lake Group Ltd., John Penney and Sons Ltd., and the assets of North Atlantic Fisheries Ltd. owned by National Sea Products and H.B. Nickerson and Sons. Ottawa would own 60 per cent and appoint five directors, Newfoundland would own 25 per cent and appoint three directors, the Bank of Nova Scotia would own 12 per cent and appoint one director, and the employees would own 3 per cent with one director. However, employees could not appoint a director unless they purchased shares in the company. The chairman and CEO were to be appointed jointly by Ottawa and St. John's. Both governments agreed to sell their shares to private interests as soon as possible. Ottawa would make a cash contribution of $75.3 million while Newfoundland and the Bank of Nova Scotia would convert to equity in the new company their loans of $31.5 million and $44.1 million respectively. Layoffs of more than 100 employees or half the workforce of any plant were to be subject to the approval of both governments. If one should oppose a layoff it must cover any losses the company would suffer in not going ahead with a planned layoff or plant closing. Presumably, if both levels oppose a planned layoff they must share these costs.

Grand Bank is to stay open for an eighteen-month assessment period; this decision indicates that the social vision of the fishery has been considered. Rather than being closed, Burin will be converted to a secondary processing or fish-cooking plant. However, this will involve a much lower level of employment. Other plants in the Maritime provinces, particularly plants of H.B. Nickerson and Son, have been closed. Fisheries policy has attempted to achieve a degree of economic efficiency while softening the social costs of adjustment.

Nova Scotia

Negotiations to restructure Nova Scotia's fishing industry revolved around the issue of public-sector versus private-sector control over the fishery, which is essentially National Sea Products Ltd. An agreement reached 30 September 1983 among the federal government, Nova Scotia

Premier John Buchanan, and the Bank of Nova Scotia unravelled when the provincial government withdrew, apparently dissatisfied with the high level of government involvement. This left Ottawa and the Bank of Nova Scotia with a 56 per cent interest in National Sea Products Ltd., the largest fish-processing company in Nova Scotia. At year-end 1983, National Sea had long-term debt of $119.4 million and assets of $270.9 million (see Table 33).

On 6 December 1983, a new proposal was presented to the federal government by a group of National Sea minority shareholders led by David Hennigar of Scotia Investments Ltd. Nova Scotia favoured the proposal as a private-sector alternative. During early negotiations, Kenneth Streatch, then Nova Scotia's minister of fisheries, stated that his government rejected Newfoundland's solution since 'the viability of the fishing industry is, indeed, there in the private sector. . . to go the route of a Crown Corporation. . . would only tend to deteriorate the potential for further development of the fishery, and would, indeed, extend a very serious blow to the competitiveness of private enterprise against a Crown Corporation.'[35] The federal negotiating team repeatedly asserted that this was a false issue since the federal government had no intention of 'nationalizing' the industry. The real issue may well have been local versus federal control of Nova Scotia's fishery.

The Hennigar proposal was rejected by the federal government and the National Sea Restructuring Committee of the board as inadequate to meet National Sea's financial needs. To permit further negotiations the Bank of Nova Scotia extended the date for foreclosure on loans to National Sea until 9 February 1984. On 6 February 1984 an agreement was reached which resulted in a $55 million equity injection by private investors and the federal and Nova Scotia governments into National Sea and completed the restructuring. Three private interests, Scotia Investments Ltd., Empire Co. Ltd., and Isleview Investments Ltd. agreed to make a direct equity contribution of $20 million and own 66 per cent of National Sea. David Hennigar, of Scotia Investments Ltd., was to be the largest single shareholder in National Sea with a 47 per cent interest, and he was to have the first right of refusal to purchase Ottawa's share when the federal government decided to sell its interest. The Nova Scotia government agreed to convert $25 million of debt in National Sea and H.B. Nickerson and Co. into National Sea nonvoting preferred shares, and will hold a 14 per cent interest in the company. Payment of

TABLE 33

National Sea Products Limited

Historical summary (as originally stated in company's annual reports for the respective years)

Year	Total assets	Working capital	L.-term debt	S.-term debt	Shldrs.' equity[a]	Net sales	Net Inc. oper.	Earns. per com. sh.	Com. Price Range High	Com. Price Range Low
	($000s)							$	$	$
1970	42,095	8,313	11,099	N.A.	14,991	64,950	1,866	1.40	10.00	6.50
1971	48,188	10,512	13,472	N.A.	16,108	63,363	1,678	1.19	11.38	7.88
1972	54,779	7,961	14,532	N.A.	20,079	69,319	1,803	1.13	10.50	7.50
1973	61,292	10,895	17,167	N.A.	22,070	89,049	3,815	2.43	18.00	9.88
1974	73,190	13,954	26,895	N.A.	21,870	90,068	d2	d0.06	16.00	5.00
1975	72,622	9,357	28,158	N.A.	20,350	97,324	d1,027	d0.75	11.00	5.50
1976	84,420	9,929	26,209	N.A.	20,504	164,429	1,490	0.90	14.00	8.63
1977	90,088	12,650	25,148	18,734	24,983	164,659	4,934	3.24	13.00	9.00
1978	120,300	15,596	26,837	28,857	33,372	217,481	9,985	2.13 b	23.00[b]	4.30[b]
1979	181,179	20,834	48,312	58,846	40,989	268,057	8,103	1.72	24.75	14.00
1980	208,915	13,215	67,319	72,812	41,513	274,447	2,484	0.51	18.00	9.00
1981	211,230	606	71,643	76,995	40,578	313,567	d1,380	d0.32	13.00	7.00
1982	291,250	22,321	106,997	101,084	41,502	386,231	937	0.18	12.25	5.75
1983	270,857	13,285	119,389	99,999	24,043	452,158	d20,278	d4.40	11.75	7.25

a Includes preference shares.

b Following 2-for-1 splits in October 1958 and February 1964 and 3-for-1 stock split in November 1978.

principal on the remaining half of its debt has been postponed for five years. The federal government agreed to purchase $10 million in NSP preferred shares, and will own 20 per cent of the company. Ottawa also agreed to give $70 million to the Bank of Nova Scotia to release it and Nickerson of its $100 million in debt obligations. H.B. Nickerson's assets will be distributed between NSP and Newfoundland's Fishery Products International. Governments thus provided 65 per cent of the financing of the new company. The Toronto-Dominion bank agreed to purchase $75 million of 'financial difficulty' preferred shares from a National Sea subsidiary. These bear interest (which is tax free) at just over half of prime, and must be bought back by NSP within five years. This money will be used to pay off the company's debt to the Bank of Nova Scotia. The Bank of Nova Scotia is pulling out of the company leaving the TD and the Royal Bank as the company's main bankers. The federal and Nova Scotia governments have each been promised seats on the company's board of directors.

One year after the release of the Kirby report, Ottawa, St. John's and Halifax completed negotiations and agreements on a radical restructuring of the Atlantic fishery. All three governments stated that they had been reluctant to take equity in the new super companies. However, 'to have injected capital without equity would have been a bailout' which none were prepared for.[36] Liquidation would otherwise have occurred since private investors had been unwilling to participate. If the merged companies had been liquidated large fish inventories would have been sold at distress prices which the independents could not have met. As Kirby stated, 'governments and the bank have simply become the buyers of last resort, a possibility we had foreseen from the beginning if no private investors could be found. And once we decided not to bail anyone out, we knew we were going to have to get something for our money and that was equity in the new company.'[37]

Backlash in the industry

Industry spokesmen have expressed their fears concerning potential unfair competition from the new super-companies. Gerry Cluney, secretary of the New Brunswick Fish Packers Association, stated that the restructuring plans resulted in 'government-created monsters' that could destroy independent processors. The fears of unfair competition were heightened when Art May, deputy minister of the federal Depart-

ment of Fisheries, stated that the restructured companies would have no set policy on profit margins.[38] Pierre De Bané had insisted that independent processors, such as those which recently formed the Federation of Independent Seafood Producers of Atlantic Canada to oppose the restructuring, will have nothing to fear since the new companies will be operated in a commercial manner.

Reaction from the United States

American fishermen were quick to react to what they perceive as a state-owned, government-subsidized Canadian industry. However, even with the large federal interest in the Newfoundland company, governments control only about a quarter of the Atlantic fishery. Nova Scotia's company is controlled almost entirely by private interests. In late November 1983 President Reagan authorized a section 332 investigation which is to report by December 1984 into the dealings of Canadian fish companies in US markets.[39] A 332 (named after a section of the 1974 Trade Act) is a factfinding study which looks into charges of unfair competition from foreign industries operating in the United States. If it finds that the Canadian competition is unfair it could trigger countervailing tariffs or duties. One of the problems the Canadian industry faced was soft US markets and poor fish prices. A tariff would deprive Canadian fish of access to the vital US markets.

CONCLUSION

It appears that the social vision – the preservation of employment – prevailed over the economic or commercial efficiency vision in the restructuring of the Atlantic fishery. The new corporate structure of the industry integrates harvesting, processing, and marketing within two of Canada's largest fishing companies which must now achieve long-term viability. The Nova Scotia company (National Sea Products Ltd.) is 20 per cent owned by governments while the Newfoundland company (Fishery Products International) is 85 per cent owned by governments. Eight of eleven directors are government-appointed, and the CEO is a joint government appointment. Although the pattern of ownership does not in itself guarantee a fishery with a less than total emphasis on commercial viability, the fact that all 'significant' corporate decisions, such as plant closures, are subject to the veto of both governments, and that management must consult the governments which must consult

each other before a business plan may be submitted to the board, is likely to detract from efficient management. The governments concerned traditionally have been inclined to act to preserve jobs in the industry rather than work towards long-run economic efficiency.

Depressed markets in the United States, where 80 per cent of Atlantic fish is sold, and fierce competition from Scandinavia have continued to contribute to severe difficulties in the Atlantic fishery. Although National Sea has proved more able than Fishery Products International to abandon marginal operations (among others the Halifax plant was closed in May 1984) and has re-aligned management, the company has experienced difficulties. NSP lost $10.6 million in the first nine months of 1984 (compared to $12.7 million over the same period in 1983) on sales of $305.7 million (compared to $347.7 million in the first nine months of 1983). While Allan Billard, executive director of the Eastern Fishermen's Federation, has stated that National Sea should be allowed to fail since small processors cannot compete,[40] David Hennigar, chairman of National Sea, maintains that NSP is viable although it may eventually require further assistance.[41]

Fishery Products International proved less able to rationalize its operations and cut operating costs. FPI was underfinanced from its creation, in part because the company had been expected to close several plants but did not for social and political reasons. Ottawa's equity infusion was used to reduce $55 million in debts to the Bank of Nova Scotia, rather than being used as operating capital as was intended.[42] FPI has accumulated $115 million in debts. The nineteen-month delay in establishing the company while Ottawa and St. John's debated, and the six-month delay in naming a board of directors, cost money ($12 million in interest charges),[43] heightened uncertainty, and hurt confidence in Newfoundland's fishery. In addition, FPIs deep-sea trawlermen went on strike in May 1984. Richard Cashin, president of the NFFAW, claimed that restructuring had failed to take into account the needs of fishermen and plant workers.[44] Industry workers have been at the same wage levels since 1982, and had been without a collective agreement for two years. Labour problems have resulted in production cuts of 15 to 20 per cent. In the face of fierce competition in the over-supplied American market FPIs strategy has been to sacrifice volume to keep prices as high as possible. The attendant heavy inventory-carrying costs have been a factor contributing to FPI's problems.

In September 1984 an order-in-council authorized a guarantee of a $25 million line of operating credit by the Bank of Nova Scotia to FPI. FPI has requested an equity infusion of $100 to $125 million over the next five years. The company lost $30 million in 1983 and expects to lose $25 million in 1984.[45] Chairman of the Board Andrew Crosbie (brother of John Crosbie, minister of justice) has forecast that, without assistance, these losses will escalate to $90 million over the next five years, while the company could break even by 1986 with an equity infusion.[46]

NOTES

1 From 36,500 to 53,500 (licensed by Ottawa). In Michael Kirby (1982) 'Navigating troubled waters'. *Report of the Task Force on the Atlantic Fisheries* December (hereinafter referred to as the Kirby Report).
2 From 519 to 700 (licensed by Newfoundland).
3 Kirby Report, 142-3.
4 As opposed to the common property notion, a property rights concept (as recommended in the Kirby Report) would guarantee fishermen their quota of fish. This would discourage, or reduce, the need for heavily concentrated early-season fishing.
5 Ibid., 49. Canada's fish industry was the world's number one exporter in 1979 (*Financial Post* 1 January 1983). The industry is Canada's third largest foreign-exchange earner after forest products and wheat.
6 The 'big four' account for 45 per cent of the groundfish caught, and 65 per cent of the processing; they market 85 per cent of the catch, and by 1982 were over $5 million in debt (*Montreal Gazette* 31 December 1982).
7 Terms of Reference, Canada Task Force on Atlantic Fisheries, 8 January 1982.
8 Kirby Report, 23. In Newfoundland, winter unemployment rates of 40 to 60 per cent exist in these communities (*Toronto Star* 2 February 1982).
9 *Montreal Gazette* 31 December 1982.
10 *Financial Post* 11 September 1982.
11 Hansard 2 December 1981.
12 *Financial Post* 11 September 1982.
13 Michael Valpy (1983) *Globe and Mail* 17 February.
14 Ibid.

15 Pierre De Bané, federal fisheries minister, was quoted as saying 'There will be no corporate welfare program,' while his Newfoundland counterpart James Morgan insisted, 'The time of the big bailouts is gone.' (*Globe and Mail* 21 December 1982)

16 *Globe and Mail* 30 March 1983.

17 *Globe and Mail* 24 November 1983.

18 *Globe and Mail* 6 April 1983.

19 In negotiations there had been infighting between Kirby and the federal Department of Fisheries. Kirby appeared insensitive to popular feeling when he approved the unilateral plan which was opposed by Newfoundland municipal leaders, the NFFAW, the companies, the Newfoundland government, provincial opposition parties and the Newfoundland people's conference of September 1982. (Michael Valpy (1983) *Globe and Mail* 25 October)

20 *Toronto Star* 5 July 1983.

21 *Globe and Mail* 5 July 1983.

22 *Globe and Mail* 6 July 1983. This was the conclusion of a Price-Waterhouse study commissioned by the federal Department of Fisheries.

23 Michael Valpy (1983) *Globe and Mail* 9 July.

24 *Toronto Star* (1983) 27 August 1983.

25 The federal government holds 48 per cent voting control in CDC which is a holding company with assets such as its shares in FPL. The CDC increasingly acted directly for FPL in financial matters, and both have been fighting to frustrate federal attempts to restructure the Newfoundland fisheries. The Bank of Nova Scotia took the CDC and FPL to court in St. John's, accusing them of attempting to hinder bank and other creditors from collecting debts by, among other things, transferring shares of FPL to a numbered company and a US subsidiary.

One theory behind a Crown corporation's attempts to thwart the federal government is that CDC's private shareholders and CEO Anthony Sampson wish to minimize Ottawa's role in the CDC and threatened to issue more preferred shares to dilute Ottawa's holding. Jack Austin, the minister responsible for CDC, got an agreement that CDC would not dilute if Ottawa did not use its share position to take part in CDCs affairs. Therefore, Ottawa can do nothing about the CDC-FPL problem. (Valpy [1983] *Globe and Mail* 20 October)

26 *Globe and Mail* 31 August 1983.

27 *Globe and Mail* 2 September 1983.
28 Ibid.
29 *Globe and Mail* 9 September 1983.
30 *Toronto Star* 26 September 1983.
31 *Globe and Mail* 16 September 1983.
32 *Toronto Star* 17 September 1983.
33 *Globe and Mail* 16 September 1983.
34 *Globe and Mail* 27 September 1983 and 25 October 1983. Ottawa had struck a new committee in early September 1983 composed of Arthur May, deputy minister of fisheries; De Bané, who was given political control (instead of Johnson); and Kirby, who negotiated with Newfoundland. Agreement was reached quickly.
35 *Nova Scotia House of Assembly Debates and Proceedings* 6 April 1983.
36 *Globe and Mail* 22 October 1983.
37 *Globe and Mail* 5 November 1983. Ottawa had injected a total of $145 million in equity in the two companies – $75 million in Newfoundland and $70 million in Nova Scotia. The two provincial governments have contributed $60 million and the Bank of Nova Scotia has put in $100 million.
38 *Globe and Mail* 2 October 1983.
39 *Globe and Mail* 25 November 1983.
40 *Toronto Star* 24 August 1984.
41 *Financial Post* 29 September 1984.
42 Ibid.
43 *Maclean's* (1984) 'A net for the fisheries', 3 December, 8j.
44 *Globe and Mail* 31 July 1984.
45 *Maclean's* 3 December 1984.
46 *Toronto Star* 20 October 1984.

APPENDIX 14-1
RECOMMENDATIONS OF THE REPORT OF THE TASK FORCE ON ATLANTIC FISHERIES, MICHAEL J.L. KIRBY, CHAIRMAN

1. Allocate non-surplus resources to foreigners as part of agreements for reciprocal fishing rights by fishing vessels across international boundaries (e.g., with Greenland in the Davis Strait).

2. Allocate resources that are currently surplus to Canadian harvesting capacity (e.g., squid) and a fixed amount of 'non-surplus' resources (e.g., cod) preferentially to those countries that maintain a satisfactory fisheries relationship with Canada (including fisheries trade and conservation). Allocations of non-surplus resources should be made after the fact – that is, in a subsequent year as a reward for satisfactory behaviour in the previous year, rather than as an incentive. In particular, the government should not negotiate access by foreign vessels to non-surplus resources in return for access to markets.

3. Pursue, on a priority basis, reductions in tariff and non-tariff barriers affecting trade in Canadian fishery products through multilateral negotiations within the framework of the General Agreement on Tariffs and Trade.

4. Permit joint venture arrangements with foreign interests where necessary – that is, in the absence of Canadian solutions to financial equity, marketing and resource supply problems – and subject to Foreign Investment Review Agency conditions appropriate to the nature of the fishing industry. For example, the FIRA assessment will require particular care to avoid the loss to Canada of value-added fish products through the export of minimally processed products to the overseas facilities of the foreign investor.

5. Permit direct sales to foreign fishing vessels 'over-the-side' (that is, by fishermen selling their catch) and 'over-the-wharf' (that is, by processors selling minimally processed product) only in pre-determined and well-defined circumstances. Direct over-the-side sales should be permitted only where insufficient Canadian processing capacity exists, or where there is no Canadian buyer for the quantity available at the negotiated price or at the domestic price generally recognized by fishermen and processors. Direct

over-the-wharf sales should be permitted only where sufficient value has been added to the product by Canadians. This will require definition of specific allowable product forms.

6. Continue and improve the process begun in 1981 by the Department of Fisheries and Oceans to identify fishermen as full-time or part-time for the purpose of tailoring policies and programs for each group.

7. Adopt the following licensing principles: (a) The licence would pertain to the individual as a quasi-property right (the licence would be on the man, not the boat). (b) The licence would specify either a limitation on the catch (sometimes called an 'enterprise allocation' or a 'quota licence') or on the catching capacity of the fisherman's vessel and gear (sometimes called an 'effort-related' licence, as now exists in, for example, the lobster fishery). (c) The licence would be divisible and transferable (that is, it could be sold or traded) subject to certain conditions; the transfer process would be supervised by a quasi-judicial board.

8. Establish a quasi-judicial Atlantic Fisheries Licence Review Board that would act in a review and appeal capacity for the current licensing system, as well as for the system of enterprise allocations and quota licences.

9. Consolidate federal management of the fisheries in the Gulf of St. Lawrence by resumption of full federal responsibility for licensing and other aspects of marine fisheries management in Québec.

10. Establish specific allocations of fish for delivery to resource-short plants in the off-peak season. The deliveries should be by a self-financing fishing company or consortium. The only government contribution to this company or consortium would be an allocation of fish. By a target date of 1987, only Canadian vessels should be permitted to catch these allocations.

11. Adopt the following criteria as the basis for selecting the plants that will qualify as resource-short. For purposes of the policy a plant will be defined as resource-short if:

    a) its principal supply of fish is from vessels of less than 65 feet;

b) the ratio of the production of the plant during its six months of greatest throughput to its production during the balance of the year is greater than a specified threshold (e.g., 5 to 1); and

c) the plant has installed, as of 1 November 1982, plate freezing and cold storage capacity and is capable, with at most minor modification, of winter operation.

It is recommended that preferential, though not exclusive, access to the special resource-short plant allocation should be reserved, with right of first refusal, for eligible plants adjacent to the northern cod stock on the east coast of Newfoundland (i.e., the shoreline of NAFO areas 2, 3K and 3L). The balance, plus any allocation refused by plants on the east coast of Newfoundland, should be available with right of first refusal to resource-short plants in all other east coast areas. Any remaining allocation for which the right of first refusal was not exercised would be available for bid by any Atlantic coast processor.

12. Allocate the Canadian quota of northern cod by 1987 approximately as follows (initial 1982 allocations shown for comparison):

	1982	1987
1 Inshore allowance	120,000 t	145,000 t
2 Existing trawler fleet[1]	187,250	145,000
3 Resource-short plants	5,250	50,000
4 Other fixed and mobile gear[2]	2,500	40,000
	215,000 t	380,000 t

1 Vessels over 100 feet.
2 Allocation in 1982 for vessels 65 to 100 feet and in 1987 to these plus new 'Scandinavian-type longliners.'
NOTE: The 1987 allocations are indicative only. The projected 380,000 Canadian quota is obviously subject to refinement. The allocations will be subject to adjustment for this reason, as well as in response to the evolution of allocation policy in consultation with the industry.

13. Conduct, through the Department of Fisheries and Oceans, an economic study of the feasibility and cost-benefit of freezing a portion of the summer inshore catch for processing in the off-season.

14. The governments of Canada, Québec and Newfoundland and Labrador should recognize the need for co-ordinated economic and social development initiatives in this area, and explore ways of jointly improving the socio-economic condition of the area. Federal co-ordinating responsibility would come under the purview of the Ministry of State for Economic and Regional Development.

15. Amend the Saltfish Act to allow the Canadian Saltfish Corporation to buy, process and market fish and fish products in addition to saltfish in that part of the Great Northern Peninsula of Newfoundland north of 50° and in Labrador and the Québec north shore of the Gulf. In particular, the Canadian Saltfish Corporation might purchase and operate plants such as the one it operated this summer at St. Anthony, though it would not have any monopoly on the purchase, processing or sale of uncured fish in this area.

16. Implement, after a one-year trial period, dockside grading and final product grading concurrently, with the latter, including the determination of grades and labelling, being used as a tool of marketing strategy.

17. Implement at the federal level, and with some practical exceptions, mandatory bleeding, gutting, icing and washing of groundfish at sea, with simultaneous and matching provincial legislation applied at the point of dockside sale.

18. Prepare a detailed infrastructure development plan on a community by community basis to support quality enhancement. There should be special emphasis on the provision of adequate ice-making facilities.

19. Incorporate quality considerations in the proposed production bonus program for fishermen (see Recommendation 40, Chapter 18).

20. Prepare a detailed quality awareness and education program to ensure that within three years all participants in the industry are

exposed to formal training in the principles, benefits and methods of treating fish as food.

21. Enforce universally the 130 mm otter trawler mesh size limit, and encourage the use of hook and line gear rather than gillnets and traps.

22. Processors should establish price differentials for landed quality, and cases where adequate differentials do not exist should be publicized.

23. Provincial governments that have not adopted collective bargaining legislation for inshore fishermen should do so. The federal government should support such collective bargaining by providing unequivocally for it, in all its forms, when new competition legislation is introduced.

24. The federal and provincial governments should study the concept of port market mediation commissions, port market authorities, or other institutions that may lead to greater order and efficiency in the port market.

25. Provincial governments should give high priority to up-grading the skills of fish plant managers and supervisors through vocational, technical and marketing training. Every effort should be made to foster a professional image of careers in the industry and to ensure that educational programs for management have a practical orientation and high performance standards.

26. The federal government should continue to re-orient its regional development assistance programming for the fish processing industry away from plant construction and expansion and toward improving the efficiency of assets now in place. Capital investment aimed at increasing productivity and obtaining higher yields should be supported.

27. The manpower training program of Employment and Immigration Canada should ensure that assistance is adequate to encourage

training for skilled positions in fish plants until such time as the industry is financially able to take full responsibility itself.

28. Future federal assistance to fish plants should require, as a pre-condition, that a productivity improvement study be carried out and a program of improvement be agreed to by plant management.

29. Fish processors and the federal government should explore all ways to encourage research and development in the industry and make every attempt to involve agencies such as the National Research Council in this endeavour.

30. The fish processing industry should develop a standard format for financial and cost accounting data so that common systems can be developed and performance standards established that are comparable throughout the industry. The federal government should be prepared to assist financially the development by industry of the necessary standards and systems.

31. The compilation and analysis of industry financial statements begun for the Task Force should be continued each year through co-operation between the Fisheries Council of Canada and the Department of Fisheries and Oceans. The federal and provincial governments and the processing industry should share the cost of the project each year.

32. License all processors of Atlantic groundfish and herring, and exporters of whole or dressed fish, as a condition of selling their products internationally and inter-provincially.

33. Require that, as final product grade standards are defined, licence holders grade products that are exported or sold inter-provincially.

34. Establish an Atlantic Fisheries Marketing Commission. This Commission would in turn create, initially, three Product Marketing Councils for (a) fresh and frozen groundfish, (b) salted and dried groundfish, and (c) herring.

35. Each export licence holder should automatically be a member of the appropriate Product Marketing Council. An Executive Committee of each Council should be composed of all exporters, or consortia of exporters, accounting for more than a specified percentage of sales, say 10 per cent. The chairman of a Council should be selected by the

federal government from a short list of nominees submitted by the members of the Council. Each Council would:

a) undertake such analysis and activity as is necessary to establish marketing strategies and market development priorities for their products;

b) identify market development and sales opportunities that cannot be readily addressed by the Council members individually, and encourage and co-ordinate such initiatives as may be appropriate to exploit the opportunities;

c) plan and undertake generic promotion;

d) make recommendations to the Minister of Fisheries and Oceans on all matters affecting final product grade standards and labelling, including standards, practical enforcement procedures and penalties, and reporting conditions;

e) make recommendations to the Minister of Fisheries and Oceans on any terms, conditions and eligibility criteria that may be associated with export licences for the Council's products; and

f) prepare reports and make recommendations to the Minister of Fisheries and Oceans on (i) the implications of the marketing strategy for final product standards and the promotion plan; and (ii) the implications of the marketing strategy for in-plant handling of fish, dockside grade standards and fishery management policies and regulations.

36. The Atlantic Fisheries Marketing Commission should be composed of members from the Product Marketing Councils, provincial governments, fishermen's and processors' organizations and the federal government. The federal government would appoint a chairman from a short list of nominees submitted by the members of the Commission. The Commission should have an Executive Committee of about ten members, including the chairmen of the Product Marketing Councils and representatives, elected annually, of the other member groups. The Commission would be supported by a secretariat, headed by an executive director. The Commission would:

a) provide secretariat and analytic services to the Product Marketing Councils;

b) co-ordinate activities among the Product Marketing Councils, especially regarding conflicts in marketing strategies between products;

c) advise the Minister of Fisheries and Oceans on the requirements for fisheries management and development policies that will promote more effective marketing;

d) on the basis of the generic promotion proposals from the Product Marketing Councils, recommend to the government the rate of assessment (by product) of a levy on domestically produced products and competing imports to finance the promotion program;

e) seek provincial support for generic promotion and co-ordinate the support of governments for such promotion;

f) assign promotion funds to the Product Marketing Councils; and

g) advise the Minister of Fisheries and Oceans on the desirability and the terms and conditions of all proposed direct sales to foreign fishing vessels (over-the-side and over-the-wharf) and arrange those sales that may be assigned to it by the Minister.

37. Enact legislation to give all necessary legal status and authority to the Atlantic Fisheries Marketing Commission.

38. Commit federal funding for a five-year campaign of generic promotion of Atlantic groundfish and herring products in North America and Europe to be carried out by the Product Marketing Councils. The total federal contribution in 1982 dollars (of constant purchasing power) would be $25 million phased over five years. Thereafter, the federal funds would return to current levels of about $400,000. The industry levy (proposed in recommendation 36) would replace federal funds as processors become more profitable. During at least the initial five-year period, the Atlantic provinces will be invited to make a contribution and to ensure that any promotion activities undertaken by them will be co-ordinated with the plans of the Commission.

39. Provide up to $25 million for the food component of the Program for Export Market Development (PEMD) to be earmarked for Atlantic groundfish and herring exporters. The spending of these funds should be treated as a 'challenge grant', being conditional upon development of satisfactory promotional and marketing programs by the industry. Perhaps 80 per cent of these funds would be recoverable through the normal repayment processes of PEMD. The money would be disbursed over eight years for (a) assistance to exporters to diversify commercial markets; and (b) for the development of the marketing capability of Atlantic groundfish and herring exporters.

40. Develop a production bonus system to supplement fishermen's incomes by rewarding desirable fishing practices. This system would permit fishermen to earn cash credits, payable in the off-season, based on such factors as the gross value of their landings, fish quality, season of catch, or gear used. It would be federally funded, with initial pilot testing during the 1985 fishing season.

41. Develop a gross income stabilization plan to smooth out the high and low points in individual gross revenues over a rolling five-year period. This plan would be based on participation by all fishermen, with funding from their contributions and from the federal government. Detailed analysis should enable a pilot program to be tested in 1985.

42. In the short term, as a transition measure, request that the Canada Employment and Immigration Commission amend the regulations governing the fishermen's unemployment insurance program to provide benefit entitlement based on the best 10 weeks fished for fishermen who fish at least 15 weeks. Other changes in regulations should include (a) greater flexibility in defining the 'fishing season' to allow those who fish exclusively during the winter months to qualify for benefits; (b) restrictions on the entrance requirements to the UI program, so that persons who fish less than 6 weeks will not qualify for benefits under the fishermen's program; and (c) revision of rules to permit boat-building during the benefit period for personal commercial use. Rules determining the net insurable earnings of boat captains should also be reviewed.

43. Adopt a 'sunset' provision in the UI regulations for self-employed fishermen so that the entire program will no longer be in force after April 1, 1988, provided that the production bonus scheme (recommendation 40) and the income stabilization scheme (recommendation 41) can be implemented fully as replacements, with general approval from participants in the industry.

44. The data base on the economic situation of individuals, households, enterprises and communities involved in the fishery must be improved and maintained. A survey of household income and expenses of fishermen along the lines conducted by the Task Force should be repeated regularly. Similar surveys are required with respect to fish plant workers. The enterprise cost and earnings surveys of the Department of Fisheries and Oceans should be placed on a consistent statistical basis for all Atlantic areas, and further data must be collected on vessel financing and loan repayment costs. Data collected by the Task Force on small fishing communities should be refined and updated. These statistical activities are necessary to ensure that an adequate information base is at hand for monitoring the condition of the industry and for future policy studies at the micro and macro-economic levels.

45. Do not establish a new general program of financial assistance for either fishermen or processors..

46. Do not provide direct special assistance for vessel acquisition or replacement, but ensure that vessels can be purchased from the most economical source, unhindered by tariff or other barriers.

47. Commend provincial loan boards for their efforts to continue to provide adequate capital funding for vessel purchase and repairs on terms appropriate to the financial conditions of fishermen. Initiate consultations between the federal and provincial governments on developing a uniform set of financial assistance policies and a possible new form of lending institution for working capital.

48. Implement immediately the assignment of transferable vessel quotas to seiners, with the initial allocation distributed on the basis of relative catches in the past three years. The program would be managed by a Board elected by current licence holders, with a federally appointed chairman.

49. Establish a five-year buy-back program for boat quotas funded by industry levies on domestic purchases and over-the-side sales. These quotas would be sold back to the remaining operators. As a starting point for discussion, a levy of $10 per tonne for domestic purchases and $25 per tonne for over-the-side sales is recommended. This, combined with fixed upper limits on over-the-side sales of 40 per cent of the seiner quota in 1983, declining to 20 per cent of the quota in 1987 (the last year of the program), would yield a total of almost $5 million over the period for buy-back purposes. The buy-back program would be managed by the same Board that manages the herring enterprise quota system. Provision should be made to ensure that, by 1987, all seiners are equipped with approved refrigeration systems.

50. Establish stringent measures to prevent mis-reporting of landings – for example, by requiring landings to be made only in the presence of a fisheries officer and by suspending or cancelling licences for mis-reporting.

51. Undertake a strictly controlled program to determine the feasibility, from both the economic and managment point of view, of launching a big-boat (seiner or trawler) fishery for mackerel.

52. Review membership on management advisory committees and, in the interest of effective communication and the serious pursuit of consensus, reduce numbers to the minimum necessary to ensure that essential interests are represented. Delegate greater responsibility to sub-committees to provide for greater efficiency and more effective representation.

53. Encourage organization of fishermen generally, as well as umbrella groupings that can represent the fisherman's viewpoint on region-wide and Atlantic-wide issues.

54. Make greater use of the Federal/Provincial Atlantic Fisheries Committee to develop policy, to harmonize programs and to resolve conflicts. This will probably require the creation of a network of sub-committees on a continuing or ad hoc basis. An important specific function of the Committee should be a continuing review and assessment of fish processing capacity to curb the tendency toward excess. The Committee should also work to harmonize the

various federal and provincial subsidy and loan programs for fishermen.

55. Create an Atlantic Fisheries Consultative Group of knowledgeable and experienced individuals. The maximum size should be 10 to 12, with occasional rotation of members. The Group would operate informally, with a mandate to advise the Minister and senior officials on major strategic issues.

56. Create mechanisms for more effective interpretation of scientific material to the concerned public and greater contact between resource biologists and fishermen's groups.

57. Pursue means to communicate policy, policy changes, and the objectives of Canadian fisheries policy more effectively to the industry and the public at large.

15
The Enterprise Development Program and the Bankruptcy Act

INTRODUCTION

Firms in financial distress that want to continue operations are faced with alternative strategies. They can apply for government assistance to restructure their physical and financial capital if they meet the criteria established by the government agency. The Enterprise Development Program (EDP) is an example of programmatic bailout assistance. Alternatively, if the firms are declared bankrupt, they can submit a proposal under the Bankruptcy Act. Finally, if the creditors are agreeable they and the company can engage in a voluntary receivership and negotiate a restructuring of claims outside of the provisions of the Bankruptcy Act. In this case study, the first two options are considered in some depth. The third, which in many ways is the most interesting, is not considered because data on these voluntary receiverships or workout proposals are not readily available.

The Enterprise Development Program was established in 1977 and its organization changed with the restructuring of the federal Department of Industry, Trade and Commerce (ITC) in 1982. To clarify the role of the EDP within ITC, a brief history of the program is presented in the first section of this case study.

The two major activities supported by the EDP are the design and development of new or improved products and processes and the adjustment of Canadian industrial and processing capabilities to changing competitive circumstances. To receive loan-insurance assistance, the

business and the project must be prospectively viable and the company must be unable to obtain alternative term financing, on reasonable terms or conditions, from normal sources.

Two samples of restructuring are analysed. Later in this case study, the rationale for EDP loan-insurance assistance and the characteristics of the firms receiving this assistance are summarized. The characteristics of the EDP sample are compared to all firms submitting proposals under the Bankruptcy Act and to a subset of accepted proposals. The two samples are similar; the firms in each are in poor financial health and either a re-organization or liquidation is in order. EDP-assisted firms do not exhibit financial viability, at least not in the short run.[1]

The sample of firms submitting bankruptcy proposals also provides some insight regarding the functioning of the bankruptcy market. A comparison of the characteristics of accepted and rejected proposals does indeed provide results which would be anticipated in a properly functioning system for the redeployment of assets.

HISTORY OF EDP

Established in 1977, the EDP evolved from the integration of several programs in ITC. These programs varied; some were narrowly focused – such as the Automobile Manufacturers' Assistance, the Pharmaceutical Assistance Act, and the Footwear and Tannery Act – some were broader-based programs – the Program for the Advancement of Industrial Technology (PAIT). The integration under the EDP aegis had several purposes beyond the co-ordination of industrial-development arrangements. First, assistance would be broadened to include firms other than large firms located in central Canada. The new EDP also wanted to bring in more private-sector participation. Decisions under EDP regulations were made by the eleven Enterprise Development Boards: ten regional and one central. Each of the boards consisted of an equal number of private- and public-sector members. The regional boards could not authorize assistance above $200,000.

The central board which handled larger submissions was divided into two committees: the Innovation Assistance Panel and the Adjustment Assistance Panel. These committees reflect the dual purposes of the EDP: to foster innovation in the design and development of new or improved products and to assist adjustment to changing competitive circumstances.

The projects funded by grants or contributions are mainly for innovation. For adjustment projects the federal government provides loans or loan guarantees as a lender-of-last-resort. Although arguably some innovations may be critical to firm survival, it is the adjustment side of the EDP that deals with bailouts.

In carrying out its responsibilities, the EDP operated with two criteria: significant burden and lender-of-last-resort. In order to qualify for a contribution or loan, a company had to show that funding was necessary or the project would not be undertaken. A project would be judged to represent a significant burden to a firm if failure of the project would place the firm in financial jeopardy, or if the project would not be undertaken because of other fund commitments. Under last-resort lending the assistance was based on the presumption that the firm had exhausted all other sources of funding.

Loan guarantees under the EDP adjustment category (sometimes referred to as corporate turnarounds) were provided to a number of industrial sectors in the economy. The actual numbers and dollar amounts of approved loan insurance by industrial sector fluctuates over time as particular industries are faced with economic hardships. In the fiscal year 1980-81 there were 151 loan-insurance approvals under the adjustment category; the dollar value of this loan insurance was approximately $231 million. The largest number of loans insured was in the textile and consumer-products sector (approximately 20 per cent), followed closely by the electrical and electronics sectors and machinery. In terms of dollars of loans insured, aerospace and marine was by far the sector with the greatest amount of loan insurance (approximately 57 per cent of the total loan insurance approved).

In the 1981/82 fiscal year there were 140 loan-insurance approvals with a dollar value of approximately $132 million. The textile and consumer-goods sector again had the largest number of approvals followed by resource industry, machinery, and electrical sectors. Machinery, resource, and aerospace sectors had the largest dollar amount of loan insurance. As of 31 March 1982, a total of $101 million in EDP loan insurance was outstanding.

The EDP was subject to a number of criticisms in the 1982 report of the Auditor General. The criticisms centred on vague responsibility and wide discretion under the program, as well as the limited evidence of monitoring to ensure compliance with conditions of the grants and/or loans. The Auditor General reported there were no operating guidelines

for the boards as to what constituted an acceptable level of risk or economic benefit for Canada.[2] Furthermore, the report suggested that when the government assumed part or full ownership in a firm, decisions on future assistance should be independent of the department.[3]

After the combination of ITC and Department of Regional Economic Expansion (DREE) into the Department of Regional and Industrial Expansion (DRIE), the EDP was also changed. Effective July 1983, the Industrial Regional Development Program (IRDP) became the core program to deliver assistance to private sector firms. It not only incorporates EDP, but also includes *inter alia* Regional Development Incentives Act (RDIA), Support for Technology Enhanced Productivity (STEP), Co-operative Overseas Market Development Program (COMDP), Institutional Assistance Program (IAP), Montreal Special Area Program, and Magdalen Islands Special Area Program. Several changes have been implemented under the new program. Private sector participation is limited to an advisory function. Unlike the EDP, the new program explicitly builds regional considerations into the calculation of assistance. The criterion of significant burden has been dropped although all assistance must represent 'significant net economic or social benefit to Canada within reasonable bounds of risk.'[4] The operationalization of significant benefit or reasonable risk are left for assessment in each case.

Two other organizational changes that affect bailouts have been promulgated. First, within DRIE, the major projects and Crown Investments Branch have been established as a separate bureau to evaluate any future large bailouts, similar to Chrysler or Massey Ferguson, which are too large to be dealt with under the programmatic structure. Secondly, the creation of the Canadian Development Investment Corporation (CDIC) will affect companies which have already received assistance. The federal government has shifted responsibility for its equity investment in Canadair, Massey-Ferguson and DeHavilland to the CDIC.[5]

EDP ASSISTANCE: RATIONALE AND FIRM CHARACTERISTICS[6]

Of the total number of companies obtaining EDP loan insurance, a subsample of bailout assistance was identified. Members of the EDP who were knowledgeable on the firms used a minimum size criteria ($100,000 in loan insurance) and the bailout definition to identify whether the assistance provided was a bailout or not. The resulting sample included instances of loan insurance; financial data and other information found

on each application form were made available on a basis which did not identify the company. The sample included sixteen applications for EDP assistance dating from December 1977 to July 1982. Some companies may have more than one loan insurance event, but this would be captured in the sample as different events with potentially different financial data.

The EDP assists firms in four ways. It provides loan insurance, direct loans (only in limited circumstances), and contributions up to 75 per cent of the costs of R&D and consultants' fees. Consultants are used to conduct studies of feasibility, product enhancement, and product development and design. Fourteen of the assistance events were given only EDP-insured loans; one was also given a direct loan and another was also given an innovation grant. Four of the events had existing EDP loans or loan insurance and applied for further assistance.

The funds obtained under EDP assistance were directed to several uses; a particular loan may be needed for more than one use. Proposed uses of portions of the loans in order of popularity for all companies are outlined in Table 34.

The amounts of the assistance ranged from $2 to $19 million, with an average size of $7.6 million. The average estimated 'amount at risk'[7] based on the financial condition of the applicants at the time of application was $2.8 million. The EDP provided an average of 58.25 per cent of total financing requirements, with the remainder being obtained from conventional sources and other government agencies. In fact, the EDP prefers to guarantee loans for fixed assets when the same bank has an operating loan with the firm. This ensures that the bank will be vigilant in its monitoring of the company's operations and thereby reduce the problem of strategic behaviour by the management. Firms were given an average of 6.84 years to repay the insured loans.

Restrictions and requirements

The EDP imposed several restrictions and requirements on the assisted firms in addition to regular financial restrictions found in loan covenants. The following undertakings are examples of the conditions attached to the assistance:

- replace or restructure management.
- change ownership.
- sell certain assets.

TABLE 34
Proposed uses of EDP assistance.

Proposed use	Number of assistance events
Working capital	12
Purchase of fixed assets	8
Repayment of outstanding liabilities[a]	6
R&D	1
Startup costs	1

a Funds are not given for this purpose exclusively; it would be associated with other purposes as well.
SOURCE: Application forms for financial assistance from the EDP.

TABLE 35
Reasons for EDP assistance.

Reason	Number of assistance events
Export potential	8
Import substitution	6
Employment	10
Regional employment	7

SOURCE: Application forms for financial assistance from the EDP.

- sell certain assets.
- close subsidiaries.
- conduct marketing and productivity studies.
- engage consultants to prepare reports.

In most cases, the EDP cited multiple objectives underlying assistance to each firm. Since the assistance events we consider are bailouts, it is expected that the EDP would be the 'lender of last resort' to a potentially viable firm. From the information provided to us, it was impossible to determine whether the loan was made as a last resort. Perhaps the justification for assistance is based on benefits to Canada. Some of the reasons given for providing assistance are outlined in Table 35.

More than half of the assistance events were undertaken for employment purposes. Of the ten assistance events for which this justification was important, seven were located in depressed regions. As firms are expected to have potential financial viability, the poor future prospects of the firms in the sample are unexpected, although their poor financial histories are not. The former may explain why the companies were unable to find alternative funding. In two of the events, operating losses were experienced for at least the two years previous to the date of application; in another three, losses were reported for the previous two years; and in four more, losses were reported in the year prior to application. Only in eight of the assistance events were there positive liquidation values, and these averaged only 20.3 per cent of the book value of the assets. At the time of the application, thirteen events included firms which were in default on their loans.

Financial ratios

Three key financial ratios, measured before assistance was provided, are calculated for the sample of assistance events and presented in Table 36.

The first ratio is referred to as a liquidity ratio and reflects the ability of the firm to meet its short-term liabilities by the liquidation of current assets. A 'rule-of-thumb' value for this ratio is approximately 2. For the firms granted assistance, this ratio is not only far below the rule-of-thumb value, it is below unity, which means that the current liabilities are not even covered in the event of a liquidation.

The second ratio is also a liquidity ratio but removes the inventory from current assets. In many instances the inventory is obsolete and its value in liquidation is very small. A reasonable value for this ratio is unity – the liabilities are covered by truly liquid current assets. For the firms granted assistance, the ratio is much less than unity. These two liquidity ratios confirm that the firms obtaining assistance were in financial difficulty.

The third ratio identifies whether the firm could pay off all of its liabilities by liquidating its total assets, which would be the case if the ratio were unity. Both elements in this ratio are measured at book values. This presents a particularly serious problem for the value of assets since their value in a sale is likely to be substantially less than the book value.[8] The ratio based on book values is just marginal but if the liquidation value of the assets were used, the ratio would be very large. This

TABLE 36
Key financial ratios

Ratio	Average for all assistance events	'Rule of thumb' benchmark
i) $\frac{\text{Current assets}}{\text{Current liabilities}}$	.744	2.0
ii) $\frac{\text{Current assets} - \text{inventory}}{\text{Current liabilities}}$	.391	1.0
iii) $\frac{\text{Total liabilities}}{\text{Total book value of assets}}$	1.010	1.0

SOURCE: Application forms for assistance from the EDP.

This ratio is consistent with the observed financial difficulty of the firms receiving assistance.

Operating results

Historical and projected operating results were available for thirteen of the sample firms for varying numbers of years prior to and following the receipt of assistance (year *t*). The data are presented in Table 37. Even with EDP assistance, four firms projected continuing losses (for two or three years), one expected to break even and only eight firms expected to be marginally profitable in the year following assistance.

Average profit margin and average available funds as a percentage of sales decline until year *t* and then improve, becoming positive in the year following EDP assistance. A similar pattern is followed by average working capital. The only ratio which shows average improvement in year *t* is working capital as a percentage of sales. This could be a result of both low sales in the event year and the availability of new EDP funds which have not yet been invested in long-term assets.

Projected improvements in the years following EDP assistance are modest. By the third year, project margins are only expected to reach 3.4 per cent on average. There also appears to be a general lack of liquidity, with working capital and overall fund availability projected to be at low

TABLE 37
Operating results – assistance-event firms.

Year	$t-2$	$t-1$	t	$t+1$	$t+2$	$t+3$
Average profit margin (in %) $= \frac{\text{net income} \times 100}{\text{sales}}$	−1.8	−6.5	−59.9	−12.0	1.7	3.4
S_{n-1}[a]	3.4	12.6	166.0	38.4	0.1	1.8
n (number of firms)	9	11	12	13	12	8
$\frac{\text{Average available funds} \times 100}{\text{sales}}$	.5	−2.6	−51.5	−8.0	4.5	6
S_{n-1}	5.7	9.1	143.7	28.7	5.1	2.8
n (number of firms)	9	11	12	13	12	8
$\frac{\text{Average working capital} \times 100}{\text{sales}}$	2.9	−1.9	−1.0	19.9	13.1	13.7
S_{n-1}	25.0	28.3	27.0	24.8	8.9	11.5
n (number of firms)	9	11	12	13	11	7
Average working capital (in $000)	1,136	943	−22.4	1,832	2,906	4,005
S_{n-1}	1,738	2,027	1,838	2,307	2,886	4,553
n (number of firms)	9	11	12	13	11	7

a Unbiased estimate of sample standard deviation.
SOURCE: Application forms for assistance from the EDP.

levels relative to sales. It appears from the available information that this sample is composed of bailouts with somewhat questionable or uncertain long-term viability.

PROPOSALS UNDER THE BANKRUPTCY ACT

In the previous section, the characteristics of the firms meeting our criterion and involved in EDP assistance were presented. Since the EDP assistance frequently requires restructuring of existing liabilities, it can be viewed as a re-organization in which the government takes over the role of the marketplace. An alternative to the government restructuring is the private-market route under the Bankruptcy Act, where a firm in

default submits a proposal for a restructuring of its outstanding liabilities. The proposal's structure is often based on the input of secured creditors, but ultimately all creditors must vote on the terms of the proposal.

To investigate the functioning of the private market, data on corporate proposals filed under the Bankruptcy Act were obtained from the Superintendent of Bankruptcy in Toronto for the fifteen-month period from April 1982 to June 1983. There were twenty-eight proposals submitted, of which eighteen were ultimately accepted by unsecured creditors. The results of the analysis should be interpreted with caution and are more impressionistic rather than statistically significant for the following reasons:

1 The companies which end up making a proposal under the Bankruptcy Act are probably an unrepresentative sample of bankrupt firms. To the extent that they qualify, these firms have probably applied for government assistance but were rejected. For whatever reason, the firms did not go the voluntary workout route. This suggests that the firms were small relative to the size normally found in the workout and the problems of moral hazard may have been serious.

2 The number of proposals is small and statistical tests are not very powerful. This becomes an even more serious problem when subsamples of accepted and rejected proposals are investigated.

Comparison of firm characteristics

In Table 38 we present a comparison of a set of characteristics of EDP assistance events and bankruptcy proposals.

The sample of bankruptcy proposals includes younger and smaller firms (as measured by the average book value of assets). The relatively poor financial condition of firms receiving EDP assistance is surprising and suggests there may be nonfinancial reasons for EDP assistance. They had a substantially higher proportion of total liabilities to the total liquidation value of their assets, relative to both the total bankruptcy proposal sample and the accepted proposals subsample.

Despite their much larger size in terms of book value of assets, the EDP sample had average net liquidation values slightly lower than the total sample of bankruptcy firms and only slightly larger than the firms with

TABLE 38
Characteristics of EDP assistance events and bankruptcy proposals

	EDP assistance	Bankruptcy proposals	Accepted bankruptcy proposals
Average age (years)	41	9.5	10.8
Size			
a) Employment (average)	1,056	n/a	n/a
b) Book value of assets (average)	$20.23 (million)	$4.19 (million)	$2.25 (million)
Financing health			
a) Total liabilities / Total assets (liquidation value)	6.04	3.31	2.71
b) Average net liquidation value	$1.95 (million)	$2.19 (million)	$1.83 (million)

SOURCE: For bankruptcy proposal: Superintendent of Bankruptcy, Toronto office. For EDP assistance: applications for assistance from EDP.

accepted bankruptcy proposals. This result could reflect either the poor financial health of EDP applicants relative to bankrupts, or the possibility that only relatively healthy firms have reason to expect that a bankruptcy proposal will be accepted by unsecured creditors. That is, the sample of firms filing bankruptcy proposals may not be representative of bankrupt firms in general.

Restructuring proposals

Is it possible to distinguish accepted from rejected proposals on the basis of differing financial and economic characteristics? In a properly functioning market for the redeployment of assets, this should be possible. Eighteen of the twenty-eight proposals were accepted by unsecured creditors.

TABLE 39
Comparison of characteristics of accepted and rejected bankruptcy proposals

Characteristics	Total sample	Accepted proposals	Rejected proposals	Difference of means; 't' statistic
n =	28	18	10	–
Total liabilities / Total assets (liquidation value)	3.31	2.71	4.24	1.37
Secured liabilities / Total liabilities	54.1%	57.6%	49.0%	3.80
Average age (years)	9.5	10.8	7.8	1.65
Number of months to final proposed dividend	12.8	10.9	21.0	3.56

SOURCE: Superintendent of Bankruptcy, Toronto office.

All of the firms in this sample were in poor financial condition. Of the eighteen accepted proposals, only four companies were expected to make any distribution to unsecured creditors in the event of bankruptcy and liquidation. Of these four, all of the expected realizations on liquidation were under 20 cents on the dollar. Of the ten rejected proposals, only two mentioned any payment to unsecured creditors in the event of bankruptcy and these were for only 7 cents and 16 cents on the dollar. As liquidation values were very low for both types of proposals, unsecured claimants had little to gain by rejecting the proposals. However, other characteristics of the sample do allow a more meaningful comparison of the two groups of firms (see Table 39).

Using a difference of means test, only two distinguishing features are statistically significant; accepted proposals were issued by firms with a higher proportion of secured to total liabilities and involved less time

until the final instalment of the distribution to unsecured creditors. Less statistically significant, but also interesting, are the following features; firms whose proposals were accepted were older, had lower ratios of total liabilities to total liquidation value of assets and tended to be involved in manufacturing activities.

Of the five firms in the total sample that already had government financial assistance (from the EDP), four proposals were accepted. Also, the insolvency of firms whose proposals were accepted was blamed less on management problems and recent investments or expansions and more on poor economic conditions compared to the insolvency of firms with rejected proposals.

These results are consistent with an efficiently operating market. Characteristics which would be perceived to reduce the risk or enhance the expected recovery for unsecured creditors were correlated with proposal acceptance. For example, a shorter time period for the proposed distribution would increase the expected present value of the unsecured claims. Older, more established firms and firms with lower ratios of total liabilities to the liquidation value of their assets would be less risky, as would firms with government financial assistance.

NOTES

1 Although it would be interesting for purposes of comparison, data is not available for firms which re-organize outside of the Bankruptcy Act and which do not employ government agency procedures or financial assistance.
2 The Auditor-General's Report 1982, 285.
3 Ibid., 278.
4 R. Fantham and P. Doherty (1984) 'Industrial Assistance Programs in Canada,' 8th ed. (Toronto: CCH Canadian Ltd.), 81.
5 For a discussion of the CDIC probable role in managing these assets, see S. Brooks (1983) 'The state as entrepreneur: from CDC to CDIC'. *Canadian Public Administration*, 26 (Winter) 525-43.
6 The authors of the study wish to thank EDP personnel for their assistance in identifying bailouts and discussing the loan-insurance assistance.
7 The amount at risk refers to the total loan insurance adjusted for the probability that the insurance would be invoked.
8 This point was discussed in some detail in Volume 1, Chapter 4.

Ontario Economic Council Research Studies

34 The Political Economy of Business Bailouts

M. TREBILCOCK, M. CHANDLER, M. GUNDERSON, P. HALPERN and J. QUINN

The *Political Economy of Business Bailouts* is an interdisciplinary study that draw on legal, economic, and political perspectives in seeking to explain the patterns of business bailouts by governments in Canada, in attempting to evaluate their costs an benefits, and in proposing alternative policy approaches to what has become a majoı policy dilemma for government. The study offers an historical sketch of the nature of the bailout phenomenon in Canada since the early years of the nineteenth century and then proceeds to evaluate possible economic justifications for government bail-outs of failing firms. Few economic justifications are found persuasive. Political explanations of business bailouts provide a possible basis for government intervention in a much wider range of cases. The economic and political frameworks of analysis are then brought to bear on fourteen case-studies of recent business bail-outs. Few can be justified in economic terms, although many more seem explicable in terms of the political framework of analysis. The study then proceeds to examine comparative bailout experience in a number of other countries, and concludes, by drawing on both Canadian and comparative experience, in offering a variety of proposals designed to render more congruent than in the past the policy outcomes suggested by sound economic analysis and those dictated mostly by political considerations.

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